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No. 1915

In the Supreme Court of the United States.

OCTOBER TERM, 1915.

THE UNITED STATES, PETITIONER,

v.

THEODORE W. WHITTEMORE, AS RECEIVER, ETC., ET AL.

THE UNITED STATES, PETITIONER,

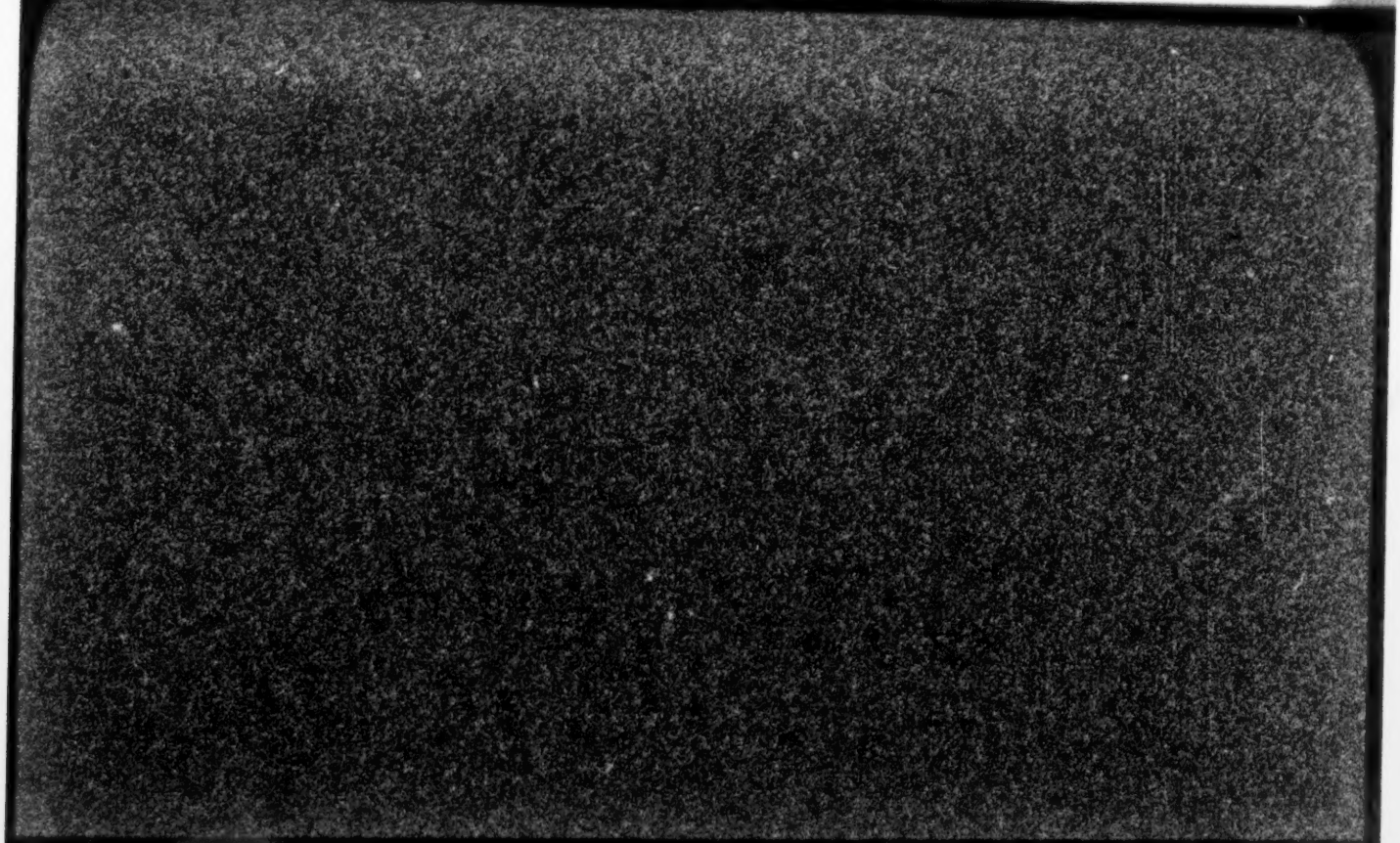
v.

ARTHUR M. JOLLEY AND DOUGLAS ROBINSON, AS RECEIVERS, ETC.

ON WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

MOTION TO ADVANCE.

WASHINGTON, GOVERNMENT PRINTING OFFICE, 1915.



In the Supreme Court of the United States.

OCTOBER TERM, 1912.

THE UNITED STATES, PETITIONER,
v.
FREDERICK W. WHITRIDGE, AS RECEIVER, etc., et al. } No. 983.

THE UNITED STATES, PETITIONER,
v.
ADRIAN H. JOLINE AND DOUGLAS ROBINSON, as receivers, etc. } No. 984.

ON WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

MOTION TO ADVANCE.

The Attorney General, on behalf of the United States, moves to advance the above-entitled cases for hearing at the next term of this court.

These cases involve the question whether, under Section 38 of the Corporation Tax Law of August 5, 1909, receivers of insolvent corporations, duly appointed by a court of equity, and subsequently carrying on the business of such corporations by order of the court, are required to make the return prescribed by paragraph 3 of said Section 38.

The question involved is evidently one of great importance to the Internal Revenue Department in the administration of the Corporation Tax Act, in view of the many large railroad and other receiverships which often continue for a period of several years, and which at times result, when so conducted by the receivers, in a net income which would be subject to taxation if the corporations had themselves through their own officers and directors conducted the business.

There are many cases of this kind involving a considerable amount of revenue, and the case is therefore one which should be determined as soon as possible by the highest authority.

Opposing counsel concur.

JAMES C. MCREYNOLDS,
Attorney General.

WILLIAM R. HARR,
Assistant Attorney General.

APRIL 7, 1913.

○

Nos. 466 and 467.

In the Supreme Court of the United States.

OCTOBER TERM, 1904.

THE UNITED STATES, PETITIONER,

v.

FREDERICK W. WHITRIDGE, AS RECEIVER OF THE THIRD AVENUE RAILROAD COMPANY, ET AL.

THE UNITED STATES, PETITIONER,

v.

ADRIAN H. JOLINE AND DOUGLAS ROBINSON, AS RECEIVERS OF THE METROPOLITAN STREET RAILWAY COMPANY, ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

BRIEF ON BEHALF OF THE UNITED STATES.

[illegible]

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CASES CITED.

In the Supreme Court of the United States.

OCTOBER TERM, 1913.

THE UNITED STATES, PETITIONER,
v.
FREDERICK W. WHITRIDGE, AS RECEIVER of the Third Avenue Railroad Company et al. } No. 466.

THE UNITED STATES, PETITIONER,
v.
ADRIAN H. JOLINE AND DOUGLAS ROBINSON, as receivers of the Metropolitan Street Railway Company et al. } No. 467.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

BRIEF ON BEHALF OF THE UNITED STATES.

STATEMENT OF THE CASE.

The defendant companies are corporations organized under the laws of the State of New York for the purpose of building, maintaining, and operating street railroads in the city of New York. (Rec., 466, pp. 9, 33; Rec., 467, pp. 6, 29, 30.) The suits in which the Third Avenue Railroad Co. and the Metropolitan Street Railway Co. are named as defendants

were brought to foreclose mortgages. The other suits were brought by general creditors.

The proceedings are fully set forth *In re Metropolitan Railway Receivership* (208 U. S., 90, 93–96).

Prior to the year 1909 a receiver or receivers had been appointed in each of the above-entitled suits; in the foreclosure suits, of the property covered by the mortgage being foreclosed; and in the general creditors' suits, of all the property of the defendants.

The orders appointing the receivers transferred to them, in the creditors' action, all the privileges, franchises, and assets of every kind of the corporations, and, in the mortgage-foreclosure cases, all such privileges, etc., as were covered by the mortgages, and authorized the receivers to run, manage, and operate the railroads, and to discharge their public obligations; and the corporations and their officers and agents were enjoined from interfering with the receivers in said management. (Rec., 466, p. 13, Exhibit A; Rec., 467, p. 11, Exhibit A.)

The receivers did, in fact, continue such operations during the years when returns under the corporation-tax act were demanded of them. The lower courts held that the corporations were not engaged in or doing business and that the receivers did not have to make any returns under the corporation-tax law.

QUESTIONS PRESENTED.

1. When a corporation is brought into a court of equity at the suit of a creditor or mortgagee, and that court in the exercise of the jurisdiction so ac-

quired appoints a receiver of all its assets, including its franchises, and authorizes the receiver to carry on all its business, which is done, is that corporation, while thus in the hands of a receiver, doing business "with the advantages which inhere in the peculiarities of corporate or joint-stock organizations of the character described"? (*Flint* v. *Stone Tracy Company*, 220 U. S., 107, 145, 146.)

2. If such corporation is doing business, is the receiver obliged to make the return provided for in section 38 of the act of August 5, 1909 (36 Stat., 112)?

I.

Such corporation is doing business within the meaning of the corporation-tax act.

It must be admitted that the business of operating surface cars as common carriers for hire over the lines of the companies was being carried on during the period of the receivership by somebody, and, of course, it must be assumed that it was being carried on lawfully. Who, then, of all the world could carry on that business lawfully during those years? Clearly nobody but the companies. They had received charters under the statutes of the State of New York which authorized a certain number of persons to "become a corporation, for the purpose of building, maintaining, and operating a railroad," and required a certificate of "the names and descriptions of the streets, avenues, and highways on which the road is to be constructed." (See General Laws N. Y., Birdseye, 3 ed.; Railroad Law, sec. 2.) The defendant

companies acquired therefore from the State a franchise, not merely to be corporations, as seems to be claimed by their counsel, but to be corporations for the purpose of operating street railroads over certain streets. By virtue of this franchise they purchased equipment, occupied certain streets, and engaged in the business of operating street railroads. When brought into court in these proceedings in the exercise of a jurisdiction which absolutely required their presence, they came in with their full corporate capacity including this franchise from the State to be railroad corporations of a certain character. In the strict exercise of its jurisdiction thus acquired by the presence of the corporations at its bar, the court appointed receivers for all their assets, including all their franchises and privileges, and the receivers proceeded under this order of court to carry on the business of running street cars on the streets of New York. Again, it must be inquired, Who was carrying on this business if not the corporations? The receivers could not lawfully do so, either as individuals or as officers of the court. The court itself could not do so, except by virtue of the jurisdiction it acquired over these corporations having these franchises which alone made such business lawful or possible. It follows, by the method of exclusion, that it was the corporations who were carrying on the business. They still retained the legal title to all the property, and the court merely assumed supervision of their business for the benefit of their creditors, and ulti-

mately of themselves and their stockholders, by putting in possession its receiver.

If the corporations themselves are not doing business under such circumstances, how could such a suit as that of *Morrison* v. *Forman* (177 Ill., 427) be sustained where a corporation *by its receiver* was permitted to condemn property? And since the defendant companies are public-service corporations, if they really ceased to carry on their public functions when receivers were appointed, it would appear to have been the duty of the State to forfeit their charters. But would any court have sustained quo warranto proceedings against them? To such a suit they would certainly answer that they were still performing their public duties through the receivers.

The argument of counsel, based upon a distinction between the primary franchise to be a corporation and the secondary franchise to operate a street railroad on certain streets of New York, is unsubstantial in its application to the case at bar. No franchise merely to be a corporation was ever granted to these companies. Their primary franchise was to be corporations of a certain character, namely, street railroad companies, with certain powers, namely, to maintain and operate street cars on certain streets of New York City. The companies, of course, may have subsequently acquired other franchises as they acquired property of all sorts, but such so-called secondary franchises they acquired, and could only acquire, pursuant to the powers conferred upon them by their original charter. A corporation can

not, any more than a natural person, be dissected and live. It is one organic whole, and it is this whole which was before the court in these proceedings and it is this whole over which the court assumed control by its receivers.

It is said that the corporations are not within the act because its terms are not applicable to the situation existing when corporations are in the hands of receivers. This claim is made on the theory that the terms "gross income," "net income," "expenses of maintenance," "interest on its bonded or other indebtedness," "amounts received by it as dividends," all refer explicitly to the corporation itself and can not be made to fit the case of a receiver. But it is submitted that in every substantial sense the income received and disbursements made by the receiver are those of the corporation itself. The receiver takes the income as a trustee, applies it first to the debts *of the corporation*, and holds the surplus *for the corporation*. Any net income over and above the expenses, debts, etc., is the equitable property of the latter. In *Philadelphia & Reading R. R. Co.* v. *Commonwealth* (104 Pa. St., 80, 82, 83) the same argument was advanced on behalf of the company as is made here, and it was thus answered by the lower court in an opinion adopted by the Supreme Court:

> It is argued by the able and ingenious counsel of the defendant, that the taxability or otherwise of the gross receipts depends upon the relation of the taxing Act of those into whose hands they come; in other words,

that the expression "gross receipts of said company" means the gross amount received by said company, and that, as the company, as such, received nothing, it had no gross receipts. We do not so understand the Act. *As we construe it, "gross receipts" is equivalent to "gross increase" or "gross earnings," and we think that their origin and ownership, rather than the hands into which they come, must be considered in determining the question whether they are taxable or not.*

How then did these gross receipts accrue, and to whom did they really belong? The franchise and privileges, the railroads and canals, the property of every kind, real and personal, though exercised, operated, and used by the receivers, were owned by the corporation defendant. *It was, then, the exercise, operation, and use of the property of defendant that produced the gross receipts, and these went into the hands of the receivers, simply because they were receivers of the property and assets of the defendant.* Their appointment gave them—so far as this case is concerned—no right to take any gross receipts that did not belong to defendant. *They were acting for it, and at its expense, and not for themselves, and the product of the exercise and use of its franchises and property belonged to it as much as the franchises and property themselves.* The only difference is that had the receivers not been appointed, the officers of the defendant would have been free to apply the receipts to such of its uses as they thought best, whereas the receivers will apply them to such of its uses as

> the court may direct. In either case they are used for the benefit of the defendant.

It may be said that the liabilities of the receiver are not the liabilities of the corporation and therefore it can not be the corporation which is carrying on the business, but this is true in only a limited sense. The corporation is not liable in a personal action, but a debt may exist without any such liability, as is shown by the early history of the pledge. The fact remains that the liabilities of the receiver are paid, not out of his own pocket, but out of the assets of the corporation, and in some cases they are made an express lien on its property. This shows that they are in a substantial, practical sense, leaving out of view any question of remedies, the liabilities of the corporation.

The Court of Appeals of New York has, in three cases, expressly construed a taxing statute in substantially all respects similar to the corporation-tax act as covering corporations in the hands of receivers.

In *Central Trust Company* v. *New York City and Northern Railroad Company* (110 N. Y., 250), the corporation-tax act of the State of New York was considered, which was before this court in *Home Insurance Company* v. *New York* (134 U. S., 594). In this latter case this court, speaking through Mr. Justice Field, said of the nature of the tax imposed, at pages 599, 600:

> It is not a tax in terms upon the capital stock of the company, nor upon any bonds of the United States composing a part of that stock.

> The statute designates it a tax upon the "corporate franchise or business" of the company, and reference is only made to its capital stock and dividends for the purpose of determining the amount of the tax to be exacted each year.
>
> By the term "corporate franchise or business," as here used, we understand is meant * * * the right or privilege given by the State to two or more persons of being a corporation; that is, of *doing business in a corporate capacity*, and not the privilege or franchise which, when incorporated, the company may exercise.

The courts of the State of New York have always adopted this same construction of the aforesaid act, and yet, in the case of the *Central Trust Company* v. *New York City and Northern Railroad Company*, *supra*, it was held that a receiver was liable for this tax. In the opinion delivered by Judge Peckham it was said (110 N. Y., 256, 257):

> * * * But we are of the opinion that the railroad when in the receiver's hands and operated by him, is operated under and by virtue of the franchise which has been conferred upon the corporation by the state, * * *. Under this order of the court he takes possession of all the property of the corporation and proceeds to operate, that is, to run its trains and to do all that was formerly done under the direction of the board of directors. In this way he uses the franchise which has been conferred by the state upon the company, and he uses it as an officer of the

> court which is administering the affairs of the company, and through the court he acts as the company to the same extent pro hac vice as if the board of directors were operating the railroad. It is the franchise which is being used in both cases, only in one case is it used for the company, and substantially by it, by means of its board of directors, while in the other case the same franchise is being used and the road is operated under it by an officer of the court until, by virtue of the legal proceedings connected with the receivership, the receiver is discharged and the road returned to its former possessors, or other proceedings taken under a reorganization, as provided by the law.

In *People ex rel Joline and Robinson as Receivers* v. *Williams* (200 N. Y., 528), the same receivers who are before this court in No. 467 by the same counsel as appear here, made the same argument as in this case against the applicability of the New York law, but the Court of Appeals overruled their claim on the authority of *Central Trust Company* v. *New York City and Northern Railroad Company, supra.*

The same ruling was made in effect in the case of the *New York Terminal Company* v. *Gaus* (204 N. Y., 512, 515), which arose under a later act laying a tax upon every corporation "for the privilege of doing business or exercising its corporate franchises in this State." In that case Judge Gray, delivering the opinion of the majority of the court, said the following:

> * * * As he had no individual interest, but only the official possession of the property, the receiver could only have operated under the corporate franchise. That he was not a general receiver, as in sequestration proceedings, but only a receiver of the mortgaged property *pendente lite*, however marked the distinction, is not material to our consideration. * * * Operation of the corporation business might have been enjoined; but from its continuance by the receiver, the legal presumption, of course, is that it was authorized. The corporation was not dissolved; its franchise to conduct the ferry business was in existence and any operation must have been by virtue of that franchise. The right of its officers to operate was taken away, for the time, by the court and was conferred upon the receiver, as its officer. Operation, therefore, could only have been under the corporate franchise, and if so, then, I think that the right of the comptroller to levy a franchise tax attached and that the tax became a lien upon the corporate assets paramount to all prior incumbrances.

It is claimed that this case was decided by a bare majority, and that the minority opinion is preferable, but it is clear that Cullen, C. J., who delivered the main dissenting opinion, did not claim that the tax was not validly imposed, but merely that it was not entitled to a preference over mortgage liens, while Chase, J., concurring with Cullen, C. J., expressly

stated that the tax was properly imposed. (204 N. Y., 523.)

It is, of course, true that the decisions of State courts are not binding on this court on the question whether a Federal tax has been validly imposed or not, but it is submitted that they are authoritative, or at any rate of great weight, on the nature of the relationship existing under State laws between a receiver and a corporation incorporated under those laws, and on the question whether such a corporation, though in the hands of a receiver, is still doing business under its State charter.

II.

The receivers must make the return provided for in the corporation-tax act.

The Circuit Court of Appeals, in holding that receivers need not make the return, put its decision on the principle that a taxing act must be strictly construed. This is true as to the persons and subjects which are claimed to be within the act, but is not true as to administrative details. In the previous argument we have demonstrated, it is hoped, that the defendant corporations are clearly within the act. That being so, the provisions of the act as to what person shall make the return on its behalf are purely administrative and should receive a beneficial rather than a strict construction. The provisions in the corporation-tax act in reference to the persons who are to make the return required thereunder were

inserted for the protection of the Government, so that those officers of the corporation who, in the general nature of things, possess the information desired, should be specifically designated. If, however, a court of equity has intervened and transferred the books and records of the corporation from the custody of its officers to the custody of an officer of said court, together with the management of the business of the corporation, and thus rendered the officers of the corporation powerless to give the required information as to the amount of its gross income, the amount of maintenance expenses, etc., the operation of the corporation-tax act should not be defeated thereby. The words of the act must be interpreted reasonably, so as to place the burden of making the return upon that person who is, by law, in possession of the information desired.

In the cases cited, *supra*, from New York and Pennsylvania, where receivers were held liable to pay certain corporation taxes, the taxing acts made no reference, in terms, to receivers, and yet the State courts did not consider this a valid objection to the application of the act to receivers.

Nor is the fact that the receiver is appointed on the ground that the corporation is insolvent any sufficient reason why he should not make a *return*. If such return fail to show the required net income, no tax accrues. On the other hand, it is common knowledge that corporations, though solvent, are forced into receiverships through the financial distress of affili-

ated companies, and, also, that corporations apparently insolvent are sometimes so carefully managed by receivers as to rehabilitate their affairs. No reason of justice excuses such corporations from the payment of this tax, merely because a court of equity has placed their affairs temporarily in the hands of an officer of such court. This would be to put the Federal Government in a worse position than the other creditors of the corporation, contrary to the general rule of the law.

It is respectfully submitted that the decrees of the court below should be reversed.

SAMUEL J. GRAHAM,
Assistant Attorney General.

OCTOBER, 1913.

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No. ~~983 and 984~~

In the Supreme Court of the United States.

CENTRAL TRUST COMPANY OF NEW YORK

against

THE THIRD AVENUE RAILROAD COMPANY AND OTHERS.

AND THREE OTHER CASES.

THE PENNSYLVANIA STEEL COMPANY

against

NEW YORK CITY RAILWAY COMPANY.

AND THREE OTHER CASES.

IN THE MATTER

of

THE APPLICATION OF THE UNITED STATES OF AMERICA FOR ORDERS DIRECTING THE RECEIVERS HEREIN TO MAKE AND FILE RETURNS UNDER THE CORPORATION TAX LAW OF THE NET INCOME OF THE CORPORATIONS OF WHICH THEY WERE APPOINTED RECEIVERS.

BRIEF ON BEHALF OF THE RESPONDENTS WHITRIDGE, JOLINE AND ROBINSON AND LADD, AS RECEIVERS, IN OPPOSITION TO APPLICATION FOR WRITS OF CERTIORARI.

EVARTS, CHOATE & SHERMAN,
Solicitors for Respondent WHITRIDGE *as Receiver.*

MASTEN & NICHOLS,
Solicitors for Respondents JOLINE *and* ROBINSON *as Receivers.*

DEXTER, OSBORN & FLEMING,
Solicitors for Respondent LADD *as Receiver.*

HERBERT J. BICKFORD,
ARTHUR H. MASTEN,
MATTHEW C. FLEMING,
Counsel.

THE EVENING POST JOB PRINTING OFFICE, 156 FULTON ST., N. Y.

In the Supreme Court of the United States.

OCTOBER TERM, 1912.

CENTRAL TRUST COMPANY OF NEW YORK
v.
THE THIRD AVENUE RAILROAD COMPANY, ET AL.

AMERICAN HAY COMPANY
v.
DRY DOCK, EAST BROADWAY AND BATTERY RAILROAD COMPANY.

THE BARBER ASPHALT PAVING COMPANY
v.
THE FORTY-SECOND STREET, MANHATTANVILLE AND ST. NICHOLAS AVENUE RAILWAY COMPANY.

THE LORAIN STEEL COMPANY
v.
UNION RAILWAY COMPANY OF NEW YORK CITY.

THE PENNSYLVANIA STEEL COMPANY ET AL.
v.
NEW YORK CITY RAILWAY COMPANY.

THE FARMERS' LOAN AND TRUST COMPANY, as Trustee, Successor of the Morton Trust Company, as Trustee,
v.
METROPOLITAN STREET RAILWAY COMPANY ET AL.

GUARANTY TRUST COMPANY OF NEW YORK
v.
METROPOLITAN STREET RAILWAY COMPANY ET AL.

THE FARMERS' LOAN AND TRUST COMPANY, as Trustee, Successor of Morton Trust Company, as Trustee,
v.
METROPOLITAN STREET RAILWAY COMPANY ET AL.

BRIEF ON BEHALF OF WHITRIDGE, JOLINE AND ROBINSON AND LADD AS RECEIVERS, IN OPPOSITION TO THE PETITION OF THE UNITED STATES FOR WRITS OF *CERTIORARI*.

The Solicitor General, on behalf of the United States, has petitioned this Court for writs of *certi-*

orari to review the decisions of the Circuit Court of Appeals for the Second Circuit (198 Fed., 774), which affirmed decrees of the District Court denying the petitions of the United States for orders to compel the respective receivers of the defendant corporations to make return for the years 1909 and 1910 of the net income for those years of said companies, pursuant to section 38 of the corporation tax law, Act of August 5, 1909, chapter 6 (36 Stat., 112).

The only question involved in the decision which the petitioner seeks to review is whether receivers of the property of corporations, appointed by a court of equity in foreclosure or general creditors' suits, are required to make the return which the Act provides shall be made by corporations under oath of their officers. The question is a simple one, dependent wholly upon the construction of the statute and the application of well established rules of law. The Act has been exhaustively and minutely considered and construed by this Court in *Flint* v. *Stone Tracy Co.*, 220 U. S., 107, and other cases decided at the same time.

These are causes where jurisdiction is dependent entirely upon diversity of citizenship, and this controversy arises under the revenue laws, and the Judicial Code contemplates that the judgments of the Circuit Court of Appeals shall be final. We know of no decision which conflicts with them, and none is referred to in the petition. They are not extraordinary nor of peculiar gravity or general importance. We do not understand that the pendency of numerous cases involving the same point has ever been recognized as ground for the issue of a writ of *certiorari*. The decisions which the petitioner seeks to review are not open to misconstruction; and, if the Government gives to them the faith and credit to which they are entitled, the numerous pending suits will be disposed of, and all cause for the conflict between administrative officers and courts administering insolvent estates, which is re-

ferred to in the petition, will be removed. These are matters wholly within the control of the Government.

STATEMENT.

Each of the above named defendants is a street surface railway corporation organized under the laws of the State of New York. The suits in which The Third Avenue Railroad Company and Metropolitan Street Railway Company are named above as defendants were brought to foreclose mortgages. The other suits were brought by general creditors. A brief history of the inception of the receiverships will be found in *Re Metropolitan Railway Receivership*, 208 U. S., 90. Prior to the year 1909, a receiver or receivers had been appointed in each of the above entitled suits; in the foreclosure suits, of the property covered by the mortgages being foreclosed; and, in the general creditors' suits, of all the property of the defendants. The order in each case authorized and directed the receivers to take possession of the railroads, franchises and other property of which they were appointed receivers, and to run, manage and operate the railroads and properties, and to collect the income thereof; and directed the officers and agents of the corporations to turn over and deliver to the receivers all property in their hands or under their control; and enjoined the corporations, their officers, directors, agents and employees and all other persons whomsoever from interfering in any way whatsoever with the possession or management of any part of the property over which the receivers were appointed.

During the whole of the years 1909 and 1910 these receivers were in the exclusive control and operation of the properties under these orders.

Each corporation, by its proper officers, made return for the year 1909 under the act in question, in which it was stated in substance that the property

of the corporation was in the hands of receivers who were in charge of its operations, and some of them also stating that they had received no income whatsoever during that year. Under instructions of the court, the receivers have made no returns (*Pennsylvania Steel Company* v. *New York City Railway Company*, 176 Fed., 471, 477).

In 1911, the United States filed petitions in the above entitled causes, praying for orders directing the receivers to make returns for the years 1909 and 1910. The Circuit Court denied these petitions (193 Fed., 286), and an appeal was taken to the Circuit Court of Appeals, which affirmed the orders appealed from (198 Fed., 774).

During the period of nearly two years which has elapsed since the Government filed its petitions, the District Court, in conformity with the views expressed in *Re Metropolitan Railway Receivership* (208 U. S., 90, 111, 112) that its possession of the property through its receivers should not be unnecessarily prolonged, has divested itself of possession and operation, through sale or otherwise, in all of the suits, except that in which the Dry Dock Company is defendant. In the Third Avenue, Forty-second Street and Union suits, the receiver has finally accounted and has been discharged. In the other suits claims to the proceeds of sale and funds in the hands of the receivers are being liquidated as fast as practicable.

FIRST POINT.

The act in question imposes a tax upon corporations for the privilege of doing business by them in their corporate capacities, based upon the net income received by them. If they do no business, they are not subject to the tax. The act does not apply to receivers of corporations.

(*a*) *Provisions and construction of the Act.*

Section 38 of the Act (36 Stat. L., 112) provides (p. 112) "That *every corporation*, joint stock company or association, organized for profit and having a capital stock represented by shares, and every insurance company, now or hereafter organized under the laws of the United States or of any State or Territory," "shall be subject to pay annually a special excise tax with respect *to the carrying on or doing business by such corporation*, joint stock company or association, or insurance company, equivalent to one per centum upon the entire net income over and above five thousand dollars *received by it* from all sources *during such year*." The Act further provides that such net income shall be ascertained by deducting from the gross income "of such corporation" expenses of maintenance and operation, losses, interest actually paid on "*its* bonded or other indebtedness," all sums "*paid by it* for" taxes, and amounts "*received by it*" as dividends upon stock of corporations subject to the tax (p. 113); that the tax shall be computed upon the remainder (after deducting $5,000) of the net income "of such corporation," and that on or before March 1, "a true and accurate return under oath or affirmation of *its president, vice-president, or other principal officer, and its treasurer or assistant treasurer*, shall be made by each of the cor-

porations," setting forth the total amount of the paid up capital stock, bonded and other indebtedness and gross income "of such corporation," and amount of dividends "received by such corporation" (pp. 114–5). Subdivision Fourth (pp. 115–6) provides for obtaining further information if the return "made by any corporation" is incorrect, by an examination of books, or attendance and examination "of any officer or employee of such corporation." Subdivision Fifth (p. 116) provides for penalties, and that all assessments shall be made and "the several corporations . . . shall be notified of the amount for which *they* are respectively liable." Subdivision Eighth (p. 117) provides that if "any of the corporations . . . shall refuse or neglect to make a return . . . or shall render a false or fraudulent return, such corporation . . . shall be liable to a penalty."

This court has held that the tax imposed by this Act is not a tax upon property, or franchises, or business, or income; but that it is a tax upon the privilege of doing business in a particular manner, namely, in a corporate capacity. If business is not done in a corporate capacity, no tax is payable.

Flint v. *Stone Tracy Co.*, 220 U. S., 107.

Even if a corporation actually receives income but does not do business, no tax is payable.

Zonne v. *Minneapolis Syndicate*, 220 U. S., 187.

Mine Hill & S. H. R. Co. v. *McCoach*, 192 Fed. Rep., 670.

It is also clear that if the corporation receives no income, it is not liable for the tax.

(*b*) *The act clearly shows on its face that Congress only had corporations in mind, and not their receivers.*

There is nothing in the Act which indicates that Congress intended to impose a tax upon receivers

of corporations. Receivers are nowhere mentioned in it. The Act imposes a tax and severe penalties for the violation of the Act. It should be strictly construed, and cannot be enlarged by construction to embrace persons or property not clearly intended to be taxed.

In *United States* v. *Harris*, 177 U. S., 305, 309, it was held that receivers were not included in the word "company" in the Act of Congress to prevent cruelty to animals while in transit, and that the act did not apply to receivers.

The Act imposes the tax upon the doing of business "by such corporation," measured by the income received "by it," and requires the return to be made by and under the oaths of certain specified *officers of the corporation.* It requires that the return shall state the income received and the specified payments made thereout by the corporation. This requirement would not be met by a return by a receiver of income received and disbursements made by him. He could not include within these headings his receipts and disbursements, nor could the officers of the corporation include in their return the receipts and disbursements of the receiver.

SECOND POINT.

The Receivers did the business of operating these railroads and received all the income thereof. The corporations did no business and received no income.

(a) *As matter of fact, none of these corporations did any business or received any income during the years 1909 and 1910.*

During the years 1909 and 1910 the receivers had exclusive possession of the property of these cor-

porations, and did and carried on all the business in respect thereof, and received all the income therefrom; and the corporations did no business, and received no income in respect of such property. This was in compliance with the orders which appointed them, and which enjoined the corporations from interfering in any way whatsoever with the possession or management of any part of the property over which the receivers were appointed. The property and the income were *in custodia legis*. The orders appointing the receivers changed the possession as well as the subsequent control and management of the property and tied the hands of the corporations in respect thereto (High on Receivers, 4th ed., § 15). It is not claimed that these corporations have violated the injunctions.

The tax is payable only in the event that the corporations did business, and also received net income in excess of $5,000. If they did no business; or, if they did business, but received no income; or, if they did no business, but received income; they are not, in any such case, liable for the tax.

The petitioner does not claim that the corporations themselves did any business or received any income; but claims that the receivers' operations and income are within the statute, upon the theory that the receivers exercised the franchises of these corporations, or must be deemed to have taken the place of the officers of the corporations.

We submit, however, that the Act applies only to an actual, not a theoretical, exercise of franchises; and to income actually received by the corporation as the result of its corporate activity (*Zonne* case, *supra*). The very object in appointing receivers is to take away from the corporations and their officers the possession and operation of their property and the receipt of the income therefrom. Therefore, it cannot be said that the corporations carried on the business done by the receivers, or received the income received by them.

The duties and functions of receivers and their re-

lation to the corporation are far different from those of officers. The primary duty of receivers is to preserve the property as a trust fund for the benefit of those who may be adjudged to have an interest in it. Operation of the property is merely incidental. Officers and directors manage it for the benefit of the corporation, and may mortgage and sell it, and declare dividends and do many other things which receivers may not do.

There is seldom any income arising during a receivership to be turned over to the corporation; but it is immaterial whether these corporations subsequently receive income which accrued during the years 1909 and 1910 or not; for the tax is imposed, not upon what a corporation may receive or be entitled to receive in the future, but upon the income actually "received *by it*" during the year for which the tax is levied. The Act contemplates that the return shall be made upon the basis of money actually received and disbursements actually made during the current year (*Mutual Benefit Life Ins. Co.* v. *Herold*, 198 Fed., 199, 216). None of these corporations received any income for the years 1909 and 1910. If any of the receivers' income should come to the corporations it would not be through their activity, and they would not be taxable (*Zonne case, supra*).

(*b*) *Corporate franchises, the exercise of which is taxable.*

A corporation carrying on a business is subject to the tax, while an individual or co-partnership carrying on the same character of business is not subject to the tax. Individuals owning and operating a street railroad would not be taxable, although their operation of the railroad would involve the exercise of franchises, that is, the right to use public streets for railroad purposes. Such franchises, (which we shall refer to as secondary franchises) may be granted to an individual, and an

"individual as well as a corporation may operate a railroad" (*People* v. *Erie Railroad Company*, 198 N. Y., 369.375). Most of the secondary franchises of these companies were originally granted to individuals. (*e. g.*, Chap. 512, Laws of 1860. Chap. 825, Laws of 1873. Chap. 361, Laws of 1863.) Such franchises cannot now be granted to individuals in the City of New York (Railroad Law, § 93); but railroad corporations may mortgage their franchises, and they may be sold to and exercised by individuals. (*People ex rel. Third Avenue R. Co.* v. *Public Service Commission*, 203 N. Y., 299, 308, which involved the sale, in one of the above entitled suits, of the property and franchises of the Third Avenue Company.)

The corporate franchise, that is, the right to do business in a corporate capacity, is wholly distinct from secondary franchises. The corporate franchise is personal in character and inalienable, and exists only during the life of the corporation. On the other hand, secondary franchises are alienable, and may exist wholly apart from a corporate franchise, and may continue after the corporation and corporate franchise have been destroyed. Railroads are operated by virtue of secondary franchises.

If, therefore, the Act imposes a tax, not upon a railroad business, but upon the doing of such business in a corporate capacity, it is clear that the only franchise the exercise of which is taxable is the corporate franchise. The right to do business in a corporate capacity has many advantages, and is a valuable right. It is only the exercise of this right that Congress intended to tax.

(c) *The Receivers never possessed or exercised the corporate franchises of these corporations.*

The corporate franchises are inalienable. The corporations could not mortgage them. Creditors could not reach them. The Court could only take such property and rights as the creditors were entitled to have applied to the payment of their debts. It could not vest corporate franchises in its

receivers. The receivers could not exercise them. How could they act in a corporate capacity? They acted as individuals, not as corporations or through corporate forms or agencies. They were the arm of the Court, acting under the orders appointing them, and not servants of the corporations. The corporations still existed, their corporate franchises were unimpaired. They retained entire control over their corporate action and agencies. They could act as freely as before the appointment of the receivers, except in so far as they were enjoined from interfering with the receivers' possession and the performance of their duties. This was not a limitation or deprivation of corporate power. The corporations were merely deprived of possession of certain property, and could not exercise their corporate powers in respect thereof. The receivers had no control over them.

The cases at bar are far different from the case of a statutory receiver, where the corporation has been dissolved and all its property and powers vested in a statutory receiver. Chancery receivers do not represent the corporation in its individual or personal character, nor supersede it in the exercise of its corporate powers, except so far as the property intrusted to their care is concerned. Notwithstanding their appointment the corporations were clothed with their franchises and still existed. They could still exercise their powers if thereby they did not interfere with the management of the railroads. They could do many corporate acts and could do all things necessary to preserve their legal existence, could sue and be sued, and were liable for their acts and upon their contracts and covenants the same as if the receivers had not been appointed.

Decker v. *Gardner*, 124 N. Y., 334.

The Court could, in a foreclosure or general creditors' suit, take possession of the secondary franchises and the receivers could exercise them.

Memphis, etc., R. Co. v. *Commissioners*, 112 U. S., 609, 619.

The possession of the railroads by the receivers gave them the power to operate them and exercise the secondary franchises which were inseparable from them. To do this they did not require and did not exercise any corporate franchises. They merely did, in their capacity as receivers, what individuals might do.

> *People ex rel. Third Avenue R. Co.* v. *Public Service Commissioners*, 203 N. Y., 299, 308.

In respect to making the returns required by the Act of 1909, the corporations did all that was within their power to do. The returns were as complete as they were capable of making them. If the petitioner had any reason for dissatisfaction, the statute gives ample remedies. The statute does not require receivers to make returns.

(*d*) *Imposition of the tax on receivers might result in a heavier tax on bankrupt estates than on going concerns for the same volume of business.*

The application of this statute to receiverships might in most instances require larger tax payments out of the property than if the same property were in the possession of the corporation. For the purpose of ascertaining the net income which is the measure of the tax, deductions are to be made from the gross income, among other things, for expenses "*actually paid within the year out of income*," for maintenance and operation, and "interest *actually paid* within the year on *its* bonded or other indebtedness." During a receivership interest is seldom paid except upon the receivers' obligations and prior liens, although the funds in hand may be sufficient to pay interest on at least some of the other indebtedness. On the other hand, corporations would almost invariably pay their interest to the full extent of their net income, and, unless hopelessly insolvent, would borrow money to pay the rest.

Again, receivers are often compelled to borrow money. Would they be entitled to deduct interest on these debts, as being interest paid on "its [the corporation's] indebtedness"? The debts of the receiver are not debts of the corporation, but are obligations incurred by the court for the payment of which it imposes a charge upon the property in its possession. Again, the large expense of a receivership for fees of receivers, counsel, masters, etc. (unlike salaries of officers and fees of counsel of a going corporation, which are paid out of income as they accrue), are not usually paid until the termination of the receivership, and then usually out of the funds in the possession of the Court, whether arising from income or the sale of the property. Thus, deductions being allowed only for payments actually made or actually made out of income, during the year, a going concern might, and usually would, be entitled to larger deductions than a receiver, although the gross income in each case might be the same. It is not conceivable that Congress ever intended any such anomaly.

THIRD POINT.

Appellant's cases distinguished.

To examine in detail each case cited in the petitioners' brief would unduly prolong this brief. As the Court below said, quoting from the opinion of LACOMBE, *J.*:

> "When it is conceded, as it must be under *Flint* v. *Stone Tracy Co.*, 220 U. S., 107, that this tax is not imposed upon the property nor upon the franchises under which the railroad is operated in the different streets and avenues, most of the cases cited by the government become inapplicable."

In re Mather's Sons' Co., 52 N. J. Eq., 607, *Chesapeake & Ohio R. Co.* v. *Atlantic Transportation Co.*, 62 N. J. Eq., 751, and *Re United States Car Co.*, 60 N. J. Eq., 514, the tax, as was stated in the case last cited, was

> "an arbitrary imposition laid upon the corporation, without regard to the value of its property or its franchises, and without regard to whether it exercises the latter or not, solely as a condition of its continued existence."

In *Philadelphia, etc., R.Co.* v. *Commonwealth*, 104 Pa. St., 80, the act provided that every railroad corporation "*owning*, operating or leasing . . . any railroad . . . shall pay . . . a tax . . . upon the gross receipts of said company for tolls or transportation." The Court held that the fact that the corporation was in the hands of receivers did not relieve the *corporation* from liability for the tax. The receivers were not parties to the action, and the question of their obligation to make the return required by the statute or pay the the tax was not involved.

New York Terminal Co. v. *Gaus*, 204 N. Y., 512, was decided by a divided Court. So far as appears from the opinions, the only question involved was whether taxes under Section 182 of the New York Tax Law were liens on the property sold at foreclosure, prior to the lien of the mortgage.

We submit that the majority opinion failed to distinguish between a tax on a franchise, and a tax on the privilege of exercising a franchise; and also failed to distinguish between a corporate franchise and a secondary franchise; and incorrectly stated the character of the franchise exercised by a receiver of mortgaged property or in insolvency. The opinion of Cullen, *Ch. J.*, in which two of his associates concurred, clearly and correctly makes these distinctions. He says (p. 519):

> "A franchise tax is of an entirely different character from a tax on property. . . .

> It is levied *on the corporation* for the privilege, as the statute declares, of carrying on its business in a corporate or organized capacity (Tax Law, Secs. 182, 184); not of doing business, *but of doing business in a corporate capacity*. . . . The decision below seems to have proceeded on the ground that the right to run a ferry was a corporate franchise granted to the corporation against whose property the mortgage was foreclosed. . . . As a matter of fact many of the ferry privileges, as well as many of the old street railroad franchises in the City of New York, were granted not to corporations but to individuals and their associates. The court below, however, considered that under our statutes individuals cannot own or operate railroads, and that, therefore, the operation of a railroad must be deemed to be under a corporate franchise, and treated a ferry franchise as analogous. If it is possible to settle any question by a uniform current of judicial authority, the settled law is clearly the reverse of the proposition asserted. From the earliest days of railroads corporations owning them have been authorized to mortgage not only the roads but the franchise to maintain and operate them. That necessarily gave to the mortgagees the right to foreclose the mortgage after default, and to the purchasers on the foreclosure the right to operate the road. No legislation could deprive them of that right. But purchasers did not, by the mortgage sale, get the right to operate the road *under a corporate existence*. . . . A receiver appointed in a foreclosure suit would take nothing by virtue of the corporate existence of the owner of the equity of redemption, but by virtue of the mortgage."

The New York Act does not contain the equivalent of the phrases which in the Federal Act are so significant of the intent to limit its operation to activities by the corporation. In *Central Trust Co.* v. *Third Avenue R. Co.*, 186 Fed., 291, it was held that the State of New York was not entitled to a

preference (the only point involved in the *Gaus* case) over the Third Avenue mortgage for franchise taxes accruing under the New York statute. A petition to this Court for a writ of *certiorari* was denied. (223 U. S., 721.)

What we have said sufficiently distinguishes the other cases involving the New York franchise tax, among them *Home Insurance Company* v. *New York*, 134 U. S., 594, and *Central Trust Co.* v. *N. Y. C., etc., R. Co.*, 110 N. Y., 250.

Spreckels Sugar Refining Co. v. *McClain*, 192 U. S., 397, did not involve the question of liability of receivers for taxes.

FOURTH POINT.

The petitions for writs of certiorari should be denied.

EVARTS, CHOATE & SHERMAN,
Solicitors for respondent, Frederick W. Whitridge, as Receiver.

MASTEN & NICHOLS,
Solicitors for respondents, Joline and Robinson, as Receivers.

DEXTER, OSBORN & FLEMING,
Solicitors for respondent, Ladd, as Receiver.

HERBERT J. BICKFORD,
ARTHUR H. MASTEN,
MATTHEW C. FLEMING,
Of Counsel.

Supreme Court of the United States.

OCTOBER TERM, 1913.

No. 1066

THE UNITED STATES,

Petitioner,

against

FREDERICK W. WHITRIDGE, as Receiver of the Third Avenue Railroad Company, and others,

BRIEF ON BEHALF OF FREDERICK W. WHITRIDGE, RECEIVER, AND WILLIAM W. LADD, RECEIVER.

JOSEPH H. CHOATE, JR.,
MATTHEW C. FLEMING,
Counsel.

THE EVENING POST JOB PRINTING OFFICE, 20 VESEY ST., N. Y.

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Supreme Court of the United States.

THE UNITED STATES,
Petitioner,

AGAINST

FREDERICK W. WHITRIDGE as Receiver of The Third Avenue Railroad Company, *et al.*,

October Term, 1913. No. 466.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit.

Brief on behalf of Frederick W. Whitridge as Receiver of The Third Avenue Railroad Company, Dry Dock, East Broadway & Battery Railroad Company, The Forty-second Street, Manhattanville & St. Nicholas Avenue Railway Company and Union Railway Company of New York City; and William W. Ladd as Receiver of New York City Railway Company.

This cause comes before this Court on a writ of *certiorari*, obtained by the United States of

America and addressed to the United States Circuit Court of Appeals for the Second Circuit, to review the decision of that court affirming a decree of the District Court denying the petition of the United States for orders to compel Frederick W. Whitridge as Receiver of The Third Avenue Railroad Company, Dry Dock, East Broadway & Battery Railroad Company, The Forty-second Street, Manhattanville & St. Nicholas Avenue Railway Company and Union Railway Company of New York City, to make return for the years 1909 and 1910, of the net income for those years of said corporations, pursuant to Section 38 of the corporation tax law, Act of August 5, 1909, Chapter 6 (36 Stat., 112).

Statement.

The respondent Whitridge was appointed receiver of the property of The Third Avenue Railroad Company (hereinafter referred to as the Third Avenue Company) covered by its First Consolidated Mortgage, dated May 15, 1900, by order of the United States Circuit Court for the Southern District of New York, dated January 6, 1908 (pp. 13-16), in a suit in equity (*Central Trust Company of New York* v. *The Third Avenue Railroad Company*) brought to foreclose said mortgage.

Mr. Whitridge was appointed temporary receiver of The Dry Dock, East Broadway & Battery Railroad Company (hereinafter called the Dry Dock Company) by order of the same Court made February 1, 1908, in a suit in equity (*American Hay Company* v. *The Dry Dock, East Broadway & Battery Railroad Company*) brought on behalf of the general creditors of the Dry Dock Company, and by decree made February 5, 1908, he was continued as receiver during the pendency of said suit.

Mr. Whitridge was appointed temporary receiver of The Forty-second Street, Manhattanville and St. Nicholas Avenue Railway Company (hereinafter called the 42nd Street Company) by order of the same Court made February 1, 1908, in a suit in equity (*The Barber Asphalt Paving Company* v. *The Forty-second Street, Manhattanville & St. Nicholas Avenue Railway Company*) brought on behalf of the general creditors of the Forty-second Street Company, and by decree dated February 5, 1908, he was continued as receiver during the pendency of said suit (pp. 19-21). On June 11, 1909, he was appointed by the same Court receiver of the property of the Forty-second Street Company covered by its Second Mortgage dated July 1, 1885, in a suit in equity brought to foreclose said mortgage (pp. 34-5) (*Union Trust Company of New York* v. *The Forty-second Street, Manhattanville & St. Nicholas Avenue Railway Company*).

Mr. Whitridge was appointed temporary receiver of the Union Railway Company of New York City (hereinafter called the Union Company) by order of the same Court made March 31, 1908, in a suit in equity (*The Lorain Steel Company* v. *Union Railway Company of New York City*) brought on behalf of the general creditors of the Union Company, and by decree dated April 6, 1908, he was continued as receiver during the pendency of said suit (pp. 21-23).

The nature of these general creditors' suits appears in *Re Metropolitan Railway Receivership*, 208 U. S., 90.

These orders and decrees authorized the Receiver to take possession of the railroads, franchises and other property of the companies of which he was appointed receiver, and to run, manage and operate the railroads and properties, and collect the income thereof; and directed the officers and agents

of the companies to turn over and deliver to the Receiver all property in their hands or under their control (pp. 15, 18, 20, 21, 23), and contained injunctive provisions (pp. 16, 18, 21, 23), of which the following is typical:

> "And the defendant, Dry Dock, East Broadway and Battery Railroad Company, and its officers, directors, agents, and employees, and all other persons claiming to act by, through, or under the defendant, and all other persons whomsoever, are hereby enjoined from interfering in any way whatever with the possession or management of any part of the property over which the Receiver is hereby appointed, or interfering in any way to prevent the discharge of his duties or his operating the same" (p. 18).

The decree in each of the general creditors' suits adjudged that the defendant "is insolvent and that its assets and property of every description constitute a fund in which the complainant and other creditors of the said defendant corporation are interested, and that the assets of said corporation should be marshaled and the extent of the rights, liens, equities, and priorities of the several creditors should be ascertained and decreed by the Court" (pp. 17, 19, 21).

During the years 1909 and 1910 Mr. Whitridge was in possession of and operated the properties of all the companies under and pursuant to the above mentioned decrees (fols. 20, 64).

On May 17, 1909, a foreclosure decree was made in the cause brought to foreclose the mortgage of the Third Avenue Company, adjudging, among other things, that there was due and owing on the bonds secured by the mortgage the sum of $40,381,173.33, being $37,560,000 for principal and $2,821,173.33 for interest, and directing a sale of the property subject to the mortgage (p. 38 *et seq.*). Pursuant to this decree the property was sold on

March 1, 1910, at public auction to James N. Wallace, Adrian Iselin and Harry Bronner, a purchasing committee of the holders of said bonds, for $26,000,000, subject to certain existing prior liens and charges. The sale was confirmed by decree dated April 13, 1910 (p. 55), which directed the Special Master, Trustee under the mortgage and Receiver to convey the property to the purchasers by deed, the form of which was approved by the decree (p. 61), and also directed the Receiver to retain possession of and operate the property until the purchasers had paid the balance of the purchase price. The decree adjudged that the purchasers were entitled to all income accruing subsequent to the date of sale not applied by him to the payment of his debts. The deed was delivered to the purchasers on April 18, 1910, and conveyed all the property of every nature and description owned by the Third Avenue Company, and all property in the possession of the Receiver, at the time of the sale (p. 65). As appears in *People ex rel. Third Avenue Railway Company* v. *Public Service Commission*, 203 N. Y., 299, these purchasers organized a new corporation to acquire the property.

On November 30, 1909, a decree was entered in the cause brought to foreclose the mortgage of the 42nd Street Company, adjudging that the amount due on the bonds secured by the mortgage was $1,670,933, of which $1,600,000 was principal and $70,933 interest, and directing that the property subject to the mortgage be sold (p. 35).

Acting under the views expressed by the Circuit Court (LACOMBE, *J.*) in *Pennsylvania Steel Company* v. *New York City Railway Company*, 176 Fed. Rep., 477, the Receiver made no returns for the years 1909 and 1910; but each corporation made return for the year 1909, in which it stated that all its property was in the possession of Mr. Whitridge as Receiver, and that it had received no income dur-

ing that year (pp. 23-32). It does not appear that the Commissioner of Internal Revenue returned any of these returns, or took any steps provided by the statute to obtain from these corporations any further return or information, or to subject them to the statutory penalties. The respondent Whitridge alleged in his answer and the allegation is not denied, that—

> "during the years 1909 and 1910 none of the said corporations of which he is receiver as aforesaid carried on or did any business in respect of the property in his possession as such receiver, respectively, and received none of the income thereof, but that all of such property was in his exclusive possession as receiver as aforesaid, and that he as such receiver managed, controlled, and operated the same and carried on and did all the business in respect thereof and received all the income arising therefrom" (fol. 64).

The respondent Ladd was appointed Receiver of New York City Railway Company in a general creditors' suit (*Pennsylvania Steel Company* v. *New York City Railway Company*), by order dated July 23, 1908, in the place and stead of Adrian H. Joline and Douglas Robinson who had been appointed Receivers of that corporation by order dated September 24, 1907 (Metropolitan Record, p. 89). The Government has not specifically asked for an order directing a return by the Receiver of the New York City Railway Company.

The Circuit Court (LACOMBE, *J.*) denied the application of the United States for an order to compel these receivers to make return for the years 1909 and 1910 (p. 71). His opinion is printed at page 66 *et seq.* of the record. The United States appealed to the Circuit Court of Appeals, which court affirmed the decree of the Circuit Court (198 Fed. Rep., 774). The opinion is printed at page 78 *et seq.* of the Record. The case comes before this court on

a writ of *certiorari* addressed to the Circuit Court of Appeals, granted on the petition of the United States.

FIRST POINT.

The act in question imposes a tax upon corporations for the doing of business by them in their corporate capacities, based upon the net income received by them. If they do no business, they are not subject to the tax. The act does not expressly apply to receivers of corporations.

(*a*) *Provisions of the Act.*

Section 38 of the Act (36 Stat. L., 112) provides (p. 112) "That *every corporation*, joint stock company or association, organized for profit and having a capital stock represented by shares, and every insurance company, now or hereafter organized under the laws of the United States or of any State or Territory . . . shall be subject to pay annually a special excise tax with respect *to the carrying on or doing business by such corporation*, joint stock company or association, or insurance company, equivalent to one per centum upon the entire net income over and above five thousand dollars *received by it* from all sources *during such year*"; that such net income shall be ascertained by deducting from the gross income "of such corporation" expenses of maintenance and operation, losses, interest actually paid on "*its* bonded or other indebtedness," all sums "*paid by it* for" taxes, and amounts "*received by it*" as dividends upon stock of corporations subject to the tax (p. 113);

> "The tax under consideration, as we have construed the statute, may be described as an excise upon the particular privilege of doing business in a corporate capacity, *i. e.*, with the advantages which arise from corporate or *quasi* corporate organization; or, when applied to insurance companies, for doing the business of such companies. As was said in the *Thomas Case,* 192 U. S., 363, *supra*, the requirement to pay such taxes involves the *exercise of privileges,* and the element of absolute and unavoidable demand is lacking. *If business is not done in the manner described in the statute, no tax is payable*" (pp. 151-2).

That the tax is not payable unless the *corporation actually carries on business,* even though it may receive income from property owned by it, is expressly decided in *Zonne* v. *Minneapolis Syndicate,* 220 U. S., 187, where the defendant, a real estate corporation, had leased its lands for 130 years, and had amended its charter so as to limit its purposes to holding title to the property, and, for the convenience of its stockholders, receiving and distributing the rents. The Court said (p. 191):

> "It had wholly parted with *control and management* of the property; its sole authority was to hold the title subject to the lease for 130 years, to *receive* and distribute the rentals which might accrue under the terms of the lease, or the proceeds of any sale of the land if it should be sold. The corporation had practically gone out of business in connection with the property and had *disqualified itself* by the terms of the reorganization from any *activity* in respect to it. We are of opinion that *the corporation was not doing business in such wise as to make it subject to the tax imposed by the act of 1909.*"

In *McCoach* v. *Minehill Railway Company*, 228 U. S., 295, a railroad corporation had leased its railroads and all property connected therewith and all its rights, powers and franchises (other than the franchise of being a corporation), and thereafter had maintained its corporate existence, received annually the rentals accruing under the lease, interest on its bank accounts, and interest and dividends on investments constituting a "contingent fund," such rentals and income amounting to about $275,000 a year, and had paid the expenses of maintaining an office and stock transfer books, including salaries of its officers and clerks, and other expenses of keeping up its corporate existence, and had distributed the residue of its receipts among its stockholders as dividends. The Court held that it was not "doing business" within the meaning of the Act. After examining at length the provisions of the Act and the earlier decisions of the Court construing it, the Court said (pp. 303-4):

> "From the facts as stated above it is entirely clear that the Minehill Company *was not*, during the years 1909 and 1910, *engaged at all in the business of maintaining or operating* a railroad, which was the prime object of its incorporation. This business, by the lease of 1896, it had turned over to the Reading Company. If that lease had been made without authorization of law, it may be that for some purposes, and possibly for the present purpose, the lessee might be deemed in law the agent of the lessor; or at least the lessor held estopped to deny such agency. But the lease was made by express authority of the State that created the Minehill Company, conferred upon it its franchise, and imposed upon it its correlative public duties. The effect of this legislation and of the lease made thereunder was to constitute the Reading Company the public agent for the operation of the rail-

> road and to prevent the Minehill Company from carrying on business in respect of the maintenance and operation of the railroad so long as the lease shall continue. And it is the Reading Company, and not the Minehill Company, that is 'doing business' as a railroad company upon the lines covered by the lease and is taxable because of it."

It is clear, therefore, that a corporation, which does no business, is not taxable under the Act, although it may own property which is being used in business by another.

The Court below did not err in its construction of the Act, as the following extracts show:

> "There can be no doubt that the special excise tax provided for by the act is imposed as a tax upon doing business in a corporate capacity" (Record, fol. 148).
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> * * * * * *
>
> "If the business be carried on by an individual or a partnership, no tax is imposed" (Record, fol. 148).
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> * * * * * *
>
> "The act, in all its provisions, clearly contemplates that the tax is to be paid by a corporation which is actually engaged in business as an actively operating concern" (fol. 149).

(c) *The Act does not mention receivers, and they are not embraced within its terms.*

There is nothing in the Act which indicates that Congress intended to impose a tax upon receivers of corporations. To construe it so as to apply to receivers would enlarge its operation so as to embrace matters not specifically pointed out, and which are not closely analogous to the objects expressly intended to be taxed.

It is elementary that a tax law applies only to such objects as are clearly embraced within its terms. It cannot be enlarged by construction to

embrace persons or property not clearly intended to be taxed.

The courts below held that the Act was not applicable to these receivers. Thus the Circuit Court (Lacombe, *J.*), in *Pennsylvania Steel Company* v. *New York City Railway Company*, 176 Fed. Rep., 477; in instructing the Receivers as to making returns under this Act, said:

> "The act contains no provisions as to receivers, and it is not thought that Congress intended to include bankrupt corporations with no net income whose properties are being administered by a court."

See also his opinion in this proceeding (fol. 124).

The Circuit Court of Appeals (COXE, *J.*), said:

> "The taxation of business done and income received by receivers is not contemplated by the act; receivers are not mentioned. This omission cannot be attributed to inadvertance. . . . Whatever the reason may have been, the fact remains that the doing of business by receivers in their representative capacity as officers of the court is not taxed by the act, and no provision is made therein for the ascertainment and collection of such a tax" (Record, fol. 147).
>
> * * * * * *
>
> "It cannot be held that an act which nowhere mentions receivers and which in every paragraph deals with corporations and joint-stock companies actually engaged in business can, by construction, be made to cover the business temporarily undertaken, of conserving the property of such a corporation for the benefit of its creditors and the public" (fol. 149).

No other conclusions would be justified. The Act declares who "shall be subject to pay" the tax, namely: "every *corporation, joint stock company*

or association . . . and every *insurance company*"; and the tax is payable "with respect to the carrying on or doing business *by* such corporation, joint stock company or association, or insurance company", measured by the income received "by it". These provisions do not embrace a receiver of any such corporation, etc., or the business done or income received by him.

The Act contains elaborate provisons for ascertaining the net income of the corporation, and requires that return shall be made by and under the oaths of certain specified *officers of the corporation*. There is no provision for a return by a receiver, and the requirements of the Act would not be met by a return by a receiver. It requires that the return shall state the income received, and the specified payments made thereout, by the corporation. The receiver could not include within these headings his receipts and disbursements, nor could the officers of the corporation include in their return the receipts and disbursements of the receiver. The Government contends that it makes no difference who makes the return. We submit that it makes all the difference in the world. The Act contemplates that the return shall be made by responsible officers of the corporation, presumably having knowledge of the facts, in order that a full and true return may be obtained, and the corporation held responsible for its contents, and penalties be imposed for false returns. Obviously, a receiver could not be subjected to the penalties imposed by the statute.

The return is to include many matters which are of no concern of a receiver, and in respect of which his information, even if he had power to obtain it, would necessarily be derived from others over whom he had no control, such as the outstanding capital stock, bonds and other indebtedness, the gross income, expenses, depreciation and the losses

of, and interest paid by, the corporation itself. Included in each one of these items there might be purely corporate transactions, having no relation whatsoever to the property in the hands of the receiver, and concerning which he would have no duty or responsibility; for the corporation might be carrying on business in respect of property not entrusted to the receiver. Thus, suppose that the Third Avenue Company had had securities not covered by its mortgage which was foreclosed, and had retained and dealt with them, as the Minehill Company retained and dealt with its "contingent fund". The Receiver could not include these in his return.

Receivers cannot be brought by construction within any of the provisions of this Act.

United States v. *Harris*, 177 U. S., 305, was an action brought against receivers of a railroad corporation to recover a penalty for a violation of the statute in relation to the transportation of livestock. The Government contended that the act was intended to apply to all common carriers and to all persons carrying on the business of common carrier. The Court said that to hold the receivers they must be regarded as embraced in the word "company," used in the act; and that that would be a strained and artificial construction; and it held that receivers were not within the terms of the act.

There is even less ground, in the provisions of the acts and their purposes, for the contention that receivers are within the scope of the act now under consideration, than there was for contending that they were within the act involved in the *Harris* case. There is no apparent reason why an act in relation to the transportation of livestock should not apply to receivers as well as to corporations; but, as pointed out in the opinions below, Congress probably intended that the Act of 1909 should not apply to bankrupt estates in the hands of the Court

for administration and distribution, both because of the nature and situation of such estates, and because it was necessary so to frame the statute that the tax could not be held to be a tax upon property within the decision in the *Income Tax Cases* (157 U. S., 429; 158 U. S., 601). The Act of 1909, like the statute involved in the *Harris* case, provides for heavy penalties; and the same rule of construction is applicable to both statutes.

We respectfully submit, therefore, that receivers of corporations are not within the terms of the Act.

SECOND POINT.

It is not the intent of the Act to impose a tax upon the doing of business by a receiver. If this were its intent, it would be unconstitutional so far as it relates to business done by receivers appointed by State Courts or under State laws, and therefore, it cannot be inferred that Congress intended to tax the business done by receivers.

If this Act applies to receivers it is either because it taxes the doing of business by a receiver, or because business done by a receiver is deemed to be business done by the corporation of which he is receiver. Of course, it cannot be sustained as a *direct* tax upon the property and income received by a receiver.

(a) The Act if applicable to receivers would apply to receivers appointed by State courts or under State laws.

The Act can apply only to receivers of corporations, joint stock companies or associations or in-

surance companies. This fact shows conclusively that Congress did not intend to tax *generally* the privilege of doing business through the medium of a receivership; but, at most, only a limited class of receiverships. It would, however, apply to receivers of such corporations and other organizations appointed by State courts and under State laws, as well as to receivers appointed by Federal courts and under Federal laws.

(b) The Act would be unconstitutional so far as it attempted to tax the privilege of doing business by State receivers.

While it may be that Congress would have had power under the Constitution to impose such an excise upon the privilege of doing business by Federal receivers, it is at least doubtful whether it would have had that power with respect to the business done by receivers appointed by State courts or under State laws.

The governmental agencies of a State cannot be taxed by the Federal Government, nor the governmental agencies of the Federal Government by a State. This applies to judicial agencies. The principle was thus stated in *Flint* v. *Stone Tracy Company, supra* (pp. 157-8):

> "The cases unite in exempting from Federal taxation the means and instrumentalities employed in carrying on the governmental operations of the State. The exercise of such rights as the establishment of a judiciary, the employment of officers to administer and execute the laws and similar governmental functions cannot be taxed by the Federal Government. *The Collector* v. *Day*, 11 Wall., 113; *United States* v. *Railroad Co.*, 17 Wall., 322; *Ambrosini* v. *United States*, 187 U. S., 1."

In *Collector* v. *Day*, *supra*, it was held that an excise could not be imposed upon the salary of a judge of a State probate court.

There is, it is true, a distinction between purely governmental activities and activities by a State which are of a private nature. This distinction was thus stated in *South Carolina* v. *United States*, 199 U. S., 437, which contains a critical examination of the leading authorities on this subject (p. 461):

> "These decisions, while not controlling the questions before us, indicate that the thought has been that the exemption of State agencies and instrumentalities from National taxation is limited to those which are of a strictly governmental character, and does not extend to those which are used by the State in the carrying on of an ordinary private business."

And in that case it was held that persons acting as agents of the State of South Carolina in selling liquor under its dispensary law were subject to the payment of the license taxes imposed by the Federal internal revenue law. Much stress was laid upon the fact that the dispensary system had been adopted largely for profit, and that the hope of profit might induce the States to take possession of all subjects of internal revenue, indeed of all property and business, and thus deprive the Federal Government of means of support, if such activities of the States be exempt from Federal taxation; and it was declared that the Constitution must be interpreted in the light of the common law and the conditions surrounding it at the time of its adoption, and that such an extension of the activities of the States were not then contemplated, and that, therefore, Congress had power to tax this business, which was of a private nature.

The business carried on by the receivers in the case at bar, was, however, of a widely different

nature. It was the performance of one of the functions of the court which was most strictly governmental in character. The power to take possession of property through the medium of a receiver, was a well recognized function inherent in courts of equity long before the Constitution was adopted. Under the more complex conditions of modern times, and especially the increase in the number and size of corporations and railroads and other public utilities, this power has been considerably extended and more frequently resorted to. In some jurisdictions it is still derived from its original source, while in others it is largely dependent upon statutes. But whatever its source, it is an important function and indispensable instrumentality of courts in the administration of the laws. In some instances executive departments of the Federal or State governments have power to take possession of assets through receivers, *e. g.*, Controller of the Currency, of national banks, and State banking or insurance superintendents of State banks and insurance companies. When the State reaches out its strong arm and takes possession of property through such receivers or through its courts and administers and distributes it to those found to be entitled to it according to its laws, can it be said to be acting in a purely private capacity? The nature and purpose of such possession are antagonistic to this idea. When a court of equity takes possession of property through a receiver, the property is deemed to be *in custodia legis*. The receiver is merely the ministerial officer or arm of the court, subject in all things to its direction and control. No court of another jurisdiction can interfere with such possession. Thus in *Porter* v. *Sabin*, 149 U. S., 473, the Court said:

> "When a court exercising jurisdiction in equity appoints a receiver of all the property

> of a corporation, the court assumes the administration of the estate; the possession of the receiver is the possession of the court; and the court itself holds and administers the estate, through the receiver as its officer, for the benefit of those whom the court shall ultimately adjudge to be entitled to it (p. 479).
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> * * * * *
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> "Until the administration of the estate has been completed and the receivership terminated, no court of the one government can by collateral suit assume to deal with rights of property or of action, constituting part of the estate within the exclusive jurisdiction and control of the courts of the other" (p. 480).
>
> *In re Tyler*, 149 U. S., 164.

While the court may exercise this jurisdiction in suits between individuals, and for the purpose of adjudicating purely private matters; and, as an incident of such possession, preservation and administration, may, and often does (particularly in case of railroads and other public utilities) actively operate the property and receive income; nevertheless, its function is purely governmental, and all property received by the receiver is received in the exercise of the power thus conferred upon him, and is held in equitable execution. The process of the court is always available to assist him and to prevent interference in the discharge of his duties. The essence and purpose of the court's action, namely, determination of the rights of claimants and preservation of the fund to meet the just claims against it, is judicial; the carrying on of the business is purely incidental to the preservation of the property. Neither the court nor the State by so doing engages in private business, in the sense of that term as employed in *South Carolina* v. *United States*. If a probate court exercises a governmental function when it administers the estate of a decedent and

adjudicates the rights of persons interested therein, it is difficult to see why a court in administering and determining the rights in respect of the property in the hands of a receiver is not equally exercising a strictly governmental function. Clearly the judicial determination of private rights is a governmental function, indispensable to the security of government and to public welfare. The power of the State may be invoked to enforce the process and decrees of its courts in suits involving purely private interests, since the determination and enforcement of such rights is a matter of the highest governmental concern. The means by which courts determine such rights and administer the law are as much instrumentalities in the administration of justice as the judge himself. The court exercises a governmental function irrespective of the nature of the litigation. If the Federal government has power to tax the privilege of doing business through the medium of a receivership, it may also tax the activities of every other instrumentality of State courts. The converse of this was thus stated by Marshall, *Ch. J.*, in *M'Culloch* v. *Maryland*, 4 Wheat., 316:

> "If the States may tax one instrument, employed by the government in the execution of its powers, they may tax any and every other instrument. They may tax the mail; . . . they may tax judicial process; they may tax all the means employed by the government to an excess which would defeat all the ends of government."

It has been the public policy to reduce rather than increase the cost of judicial proceedings. A tax upon judicial instrumentalities should be exacted only when the intent to tax clearly appears.

We respectfully submit, therefore, that, in view of the foregoing considerations, Congress did not

intend to apply this tax to the doing of business by a receiver, whether appointed by Feredal courts or State courts. Of course, Congress had power to impose a *direct* tax upon property or income received by receivers, but this Act would not be effective for that purpose.

THIRD POINT.

These Receivers did the business of operating these railroads and received all the income thereof. The corporations did no business and received no income. Business done by the Receivers cannot be regarded as business done by the corporations. The Courts below did not err in holding that the Receivers could not be compelled to make the return or to pay any tax.

(*a*) *As matter of fact, none of these corporations did any business or received any income during the years 1909 and 1910.*

Each corporation of which Mr. Whitridge was Receiver made return for the year 1909, in which it stated that it did not have possession of any of its property and had received no income (pp. 23-32). The Receiver alleged in his answer, and the allegation is not denied, that during the years 1909 and 1910, he had exclusive possession of the property of these corporations and did and carried on all the business in respect thereof, and received all the income therefrom, and that the corporations did no business, and received no income in respect of such property (fol. 64).

The orders appointing the Receiver in each case appointed him receiver of the property specified in the order, *and of the income thereof*, and authorized him "*to run, manage and operate*" the property and collect the income thereof, and directed the corporation, its "officers, directors, agents, and employees and all other persons whomsoever, * * * to turn over and deliver to said Receiver," the property of the corporation, and enjoined them from "interfering in any way whatever, with the possession or management of any part of the property over which the Receiver is hereby appointed" (fols. 29-31). The property and the income were *in custodia legis*. The orders appointing the Receiver changed the possession as well as the subsequent control and management of the property and tied the hands of the corporations in respect thereto (High on Receivers, § 15). It is not claimed that these corporations have violated the injunctions. As a matter of fact, they have done no business and have received no income; and we submit that, as matter of law, they have done no business and have received no income; and that neither the corporations nor the Receiver has exercised any franchise the exercise of which is taxable under the Act.

We submit that these corporations were more completely divested of their property and the operation and maintenance thereof and the carrying on of their business, than were the corporations involved in the *Zonne* and *Minchill* cases, *supra;* and their actual activities were much more restricted, because they retained possession and control of no property, and received no income, whatever.

The tax is payable only in the event that the corporations did business, and also received net income in excess of $5,000. If they did no business; or, if they did business, but received no income; or,

if they did no business, but received income; they are not, in any such case, liable for the tax.

We understand that the appellant does not contend that the corporations themselves did any business or received any income, but that the Receivers' operations and income are within the statute, upon the theory that the Receiver exercised the franchises of these corporations.

We submit, however, that the Act applies only to an actual, not a theoretical, exercise of corporate franchises; and to income actually received by the corporation as the result of its corporate activity. And this is the effect of the decisions in the *Zonne* and *Minchill* cases. The very object of appointing these receivers was to take away from the corporations the possession and operation of their property and the receipt of the income therefrom. That a receiver does not take the place of the officers of the corporation, and is not its agent, we shall attempt to show later.

(*b*) *Corporate franchises, the exercise of which is taxable.*

A corporation carrying on a business is subject to the tax, while an individual or co-partnership carrying on the same character of business is not subject to the tax. Individuals owning and operating a street railroad would not be taxable, although their operation of the railroad would involve the exercise of franchises, that is, the right to use public streets for railroad purposes. Such franchises (which we shall refer to as secondary franchises), may be granted to an individual, and an "individual as well as a corporation may operate a railroad" (*People* v. *Erie Railroad Company,* 198 N. Y., 369-375). Most of the secondary franchises of these companies were originally granted to individuals. (*e. g.,* Chap. 512, Laws of 1860. Chap. 825, Laws of 1873. Chap. 361, Laws of 1863.) Such

franchises cannot now be granted to individuals in the City of New York (Railroad Law, § 93); but railroad corporations may mortgage their franchises, and they may be sold to and exercised by individuals. (*People ex rel. Third Avenue Railway Company* v. *Public Service Commission*, 203 N. Y., 299, 308, which involved the sale of the property and franchises of the Third Avenue Company.) The State might destroy the corporate franchise, but it has no power to destroy the secondary franchises (*People* v. *O'Brien*, 111 N. Y., 1).

The corporate franchise, that is, the right to do business in a corporate capacity, is wholly distinct from secondary franchises. The corporate franchise is personal in character and inalienable, and exists only during the life of the corporation. On the other hand, secondary franchises are alienable, and may exist wholly apart from a corporate franchise, and may continue after the corporation and corporate franchise have been destroyed. Railroads are operated by virtue of secondary franchises.

If, therefore, the Act imposes a tax, not upon a railroad business, but upon the doing of such business in a corporate capacity, it is clear that the only franchise the exercise of which is taxable is the corporate franchise. The right to do business in a corporate capacity has many advantages, and is a valuable right. It is only the exercise of this right that Congress intended to tax.

These distinctions were clearly recognized in *McCoach* v. *Minehill Railway Company*. The Minehill Company had leased all its railroads and franchises (except its franchise to be a corporation) to the Reading Company. The Court held that the Reading Company was doing the business and was taxable because of it; but that the Minehill Company, even though it retained its corporate franchise, and did such acts as were necessary to maintain its corporate existence and receive the ordi-

nary fruits that arose from the ownership of its property, was not doing business within the meaning of the Act. It would necessarily follow if the lessee of its railroads had been an individual and the business had been carried on in any other than a corporate capacity, no tax would have been payable.

(c) *The Receivers never possessed or exercised the corporate franchises of these corporations.*

The corporate franchises are inalienable. The corporations could not mortgage them. Creditors could not reach them. The court could only take such property and rights as the creditors were entitled to have applied to the payment of their debts. It could not vest corporate franchises in its receivers. The receivers could not exercise them. How could they act in a corporate capacity? They acted as individuals, not as corporations or through corporate forms or agencies. They were the arm of the court, acting under the orders appointing them, and not servants of the corporations. The corporations still existed; but they could not interfere with the receivers' possession and the performance of their duties, and could not exercise their corporate powers in respect of their property. In the cases at bar the appointment of receivers left these corporations mere shells, stripped of all their properties; but they, and they alone, possessed their corporate franchises. When the property of the Third Avenue Company was sold and conveyed under the decree that corporation still existed and possessed its corporate franchise; but all of its secondary franchises with the right to operate them passed to the purchasers. The Receiver had possessed and operated all that thus passed by the sale, and no more. The new corporation did not succeed to the corporate franchise of the old Third

Avenue Company (*People ex rel. Schurz* v. *Cook*, 110 N. Y., 443; S. C., 148 U. S., 397).

The cases at bar are far different from the case of a statutory receiver, where the corporation has been dissolved and all its property and powers vested in a statutory receiver. Chancery receivers do not represent the corporation in its individual or personal character, nor supersede it in the exercise of its corporate powers, except so far as the property intrusted to their care is concerned. Notwithstanding their appointment the corporations were clothed with their franchises and still existed. They could still exercise their powers if thereby they did not interfere with the management of the railroads. They could do many corporate acts and could do all things necessary to preserve their legal existence, could sue and be sued, and were liable for their acts and upon their contracts and covenants the same as if the receivers had not been appointed.

Decker v. *Gardner*, 124 N. Y., 334.

The Court could, in a foreclosure or general creditors' suit take possession of the secondary franchises and the receivers could exercise them.

Memphis & Little Rock Railroad Company v. *Commissioners*, 112 U. S., 609, 619.

The possession of the railroads by the receivers gave them the power to operate them and exercise the secondary franchises which were inseparable from them. To do this they did not require and did not exercise any corporate franchises. They merely did, in their capacity as receivers, what individuals might do.

People ex rel. Third Avenue Railway Company v. *Public Service Commissioners*, 203 N. Y., 299, 308.

The Government contends that corporate franchises and secondary franchises are inseparable. In other words, that no franchises merely to be corporations were ever granted to these corporations, but franchises to be corporations to maintain and operate railroads in certain streets. It is stated at page 3 of the Government's brief that "They had received charters under the statutes of the State of New York which authorized a certain number of persons to 'become a corporation, for the purpose of building, maintaining and operating a railroad', and required a certificate of 'the names and descriptions of the streets, avenues, and highways upon which the road is to be constructed' ". The charters of these corporations are not before this Court. It is pure assumption on the part of the Government that they are of the character thus described. The Union Company's charter was granted by special statutes (Chap. 361, Laws of 1863; Chap. 340, Laws of 1892). The provision of the present Railroad Law (§ 2) that the certificate shall contain "the names and descriptions of the streets", etc., was first inserted in the statute in 1884 (Chap. 252, Laws of 1884). All the other corporations of which Mr. Whitridge is receiver were organized before that time. The Third Avenue Company was organized in 1853 and its secondary franchises were granted by The City of New York to Van Schaick and others in 1852 (*People ex rel. Third Avenue Railroad Company* v. *Newton*, 112 N. Y., 396). The franchises of the Dry Dock Company were granted by Chap. 512, Laws 1860, and other statutes, and those of the Forty-second Street Company by Chap. 825, Laws 1873, and other statutes. In most instances these grants were to individuals, who assigned them to the corporations when organized. But even if the statute had required such matter to be included in the charter, whether a certificate of incorporation or a statute, the corpora-

tion would not thus or thereby acquire its secondary franchise. Under the Constitution of the State of New York the municipal authorities have the exclusive right to grant the privilege of maintaining and operating railroads in the streets; that is, the secondary franchises (Constitution, Art. III, § 18. *People* v. *O'Brien*, 111 N. Y., 1).

The Government's contention that neither the Court nor the Receivers could carry on the business, and that it could be carried on lawfully only by the corporations, is based upon the same fallacy of the unity of the two franchises. This is in direct conflict with the decision in *People ex rel. Third Avenue Railroad Company* v. *Public Service Commission*, and *McCouch* v. *Minehill Railroad Company*, *supra*, both of which recognize a possible separate ownership and exercise of these two classes of franchises.

In respect to making the returns required by the Act of 1909, the corporations did all that was within their power to do. The returns were as complete as they were capable of making them. If they were incomplete or false, the statute gives ample remedies. The statute does not require receivers to make returns.

(d) The Receiver did not take the place of the corporation or its officers, and was not its agent.

It is alleged in the petition (fol. 21) that the Receiver by virtue of this appointment "took the place of the directors and officers of the said companies during the pendency of the above-entitled actions to the same effect and with the same liabilities, obligations, and duties as were and are imposed by law upon such directors and officers of each of said companies, and more particularly by the provisions of the said section."

It is elementary that a receiver does not take the place of and is not subject to the same liabili-

ties, obligations and duties as the directors and officers of a corporation. He is merely the officer or arm of the Court, and has only such powers and duties as are granted and imposed by the order of the Court. He is not the agent or representative of any party to the action, but is an officer of the court exercising his functions for the common benefit of whoever may ultimately be adjudged to be entitled to the property. (*White* v. *Ewing*, 159 U. S., 36.) The corporation is not responsible for his acts, a most important element of agency. There may be, and usually are, debts and obligations of the corporation which are not obligations of the receiver or payable out of the property in his hands. The corporation is still capable of doing business and incurring obligations, except in respect of the receivership property (*Decker* v. *Gardner, supra*). A receiver's powers and duties are very different from those of directors and officers. He may be temporarily entrusted with the management and operation of the property, but that is only an incident of his main function, namely, to preserve the property pending the sale or disposition of it by the court, and to receive the income for the benefit of the creditors. The corporation may or may not be found to be entitled to share in the distribution. Of course, the income cannot be taxed under the Act of 1909 by *reason of ownership*. The duties of the officers and directors are prescribed by law and the by-laws of the corporation, and they are the instrumentalities through which *the corporation acts*. They may mortgage or sell the property, buy other property, declare dividends and do many other things which a receiver may not do.

As Lacombe, *J.*, said, after remarking that "this tax is not imposed upon the property *nor upon*

the franchises under which the railroad is operated in the different streets and avenues" (fol. 124):

> "Receivers are sometimes referred to as the representatives of the corporations, but that expression is not exactly accurate. In receiverships of this sort the corporate life still continues, the corporation may go on electing officers and preserving its organization. Its property (including the franchises under which its road is operated) has been seized by the Court, and is held for the benefit of creditors or persons entitled to it; sometimes the property thus seized is sold by order of the Court *but such sale does not include the franchise of the debtor to be a corporation and to do business in a corporate capacity with the privileges thereby secured to it*, as pointed out in *Flint* v. *Stone Tracy Co., supra*, p. 161."

(c) *Income received by a receiver is not to be deemed to have been received by the corporation.*

The income collected by the Receiver belongs not to the corporation, but to whomever may ultimately be adjudged to be entitled to it. Receivers are appointed in order that the Court may take the income and apply it. There is seldom any income to be turned over to the corporation. In the case of the Third Avenue Company the property sold for many millions less than the mortgage debt, and the company will not receive back a dollar of property or income. The record does not disclose whether this will be the case of each of the other corporations. But the tax is imposed, not upon what a corporation may hereafter receive or be entitled to receive, but upon the income "received *by it*" "*within the year*" for which the tax is levied. None of these corporations received or became entitled to any income for the years 1909 and 1910.

The corporations ceased to have control and man-

agement of their property and business, and have been disqualified by injunction from doing any business in respect of the property in the possession of the Receiver and from receiving the income which the government seeks to tax. It is clear that the income received by the Receiver was not received by the corporations and did not arise from business done by them. The "tax is imposed, not upon the franchise of the corporation," nor upon its property or income; but "upon the doing of business in a corporate capacity," and the income received is merely the measure of the tax. It is not a tax upon income. The Act would be unconstitutional if it were (*Flint case, supra*). There must be "activity" by the corporation, and if it receives income without actively doing business it is not liable for the tax (*Zonne* and *Minchill* cases, *supra*).

(f) Imposition of the tax on receivers might result in a heavier tax on bankrupt estates than on going concerns for the same volume of business.

The application of this statute to receiverships might in most instances require larger tax payments out of the property than if the same property were in the possession of the corporation. For the purpose of ascertaining the net income which is the measure of the tax, deductions are to be made from the gross income, among other things, for expenses "*actually paid within the year out of earnings*," for maintenance and operation, and "interest *actually paid* within the year on *its* bonded or other indebtedness." During a receivership interest is seldom paid except upon the prior liens and the receiver's obligations, although the funds in hand may be sufficient to pay interest on at least some of the other indebtedness. On the other hand, corporations would almost invariably pay their interest to the full extent of their net income, and, unless hopelessly insolvent, would bor-

row money to pay the rest. Again, receivers are often compelled to borrow money. Would they be entitled to deduct interest on these debts, as being interest paid on "its [the corporation's] indebtedness"? The debts of the receiver are not debts of the corporation, but are obligations incurred by the court for the payment of which it imposes a charge upon the property in its possession. Again, the large expenses of a receivership for fees of receivers, counsel, masters, etc. (unlike salaries of officers and fees of counsel of a going corporation, which are paid out of income as they arise), are not usually paid until the termination of the receivership, and then usually out of the funds in the possession of the court, whether arising from income or the sale of the property. Thus, deductions being allowed only for payments actually made or actually made out of income, during the year, a going concern might, and usually would, be entitled to larger deductions than a receiver, although the gross income in each case might be the same. Congress never intended any such anomaly.

FOURTH POINT.

Appellant's cases distinguished.

The courts below distinguished the cases cited by the Government, as follows (fols. 124, 150):

> "When it is conceded, as it must be under *Flint* v. *Stone Tracy Co.*, 220 U. S., 107, that this tax is not imposed upon the property nor upon the franchises under which the railroad is operated in the different streets and avenues, most of the cases cited by the Government became inapplicable."

Furthermore, some of these cases involved taxes upon franchises, irrespective of their exercise or use in business. None of them was a tax upon the doing of business in a corporate capacity as distinguished from the franchise or right. The business done or capital employed was merely the measure of the tax. In the Government's brief in this Court, which was not received until October the 6th, after our brief had been written, the only cases involving the liability of receivers for state franchise taxes which are cited are *Philadelphia & Reading Railroad Company* v. *Commonwealth*, 104 Pa. St., 80, 85; *Central Trust Company* v. *New York City and Northern Railroad Company*, 110 N. Y., 250; *People ex rel. Joline, et al., as Receivers of The Metropolitan Street Railway Company* v. *Williams*, 200 N. Y., 528; and *New York Terminal Company* v. *Gaus*, 204 N. Y., 512.

The act involved in *Philadelphia & Reading Railroad Company* v. *Commonwealth*, 104 Pa. St., 80, provided that every railroad corporation "*owning*, operating or leasing . . . any railroad . . . shall pay . . . a tax . . . *upon the gross receipts* of said company for tolls or transportation." The court treated it as a direct tax on the gross receipts, and held that the fact that the corporation was in the hands of receivers did not relieve *the corporation* from liability for the tax. The receivers were not parties to the action, and the question of their obligation to make the return required by the statute or pay the tax was not involved. In *Philadelphia Steamship Company* v. *Pennsylvania*, 122 U. S., 326, this Court held that a "similar act" (p. 327) imposed a tax "directly upon the receipts" (p. 335) and not upon the franchise (p. 342); and was a regulation of interstate commerce, and therefore unconstitutional (p. 347). Clearly, the tax involved in the *Reading* case was not a tax upon the

doing of business in a certain capacity, measured by the income received by the corporation. The act imposed a direct tax on the gross receipts. Therefore this was really a property tax, for which the corporation owning the property, and the receiver who had possession of it, and indeed the property itself, however it might be situated, might be liable.

The statutes of the State of New York imposing taxes on corporations have been frequently amended, and the decisions have been conflicting, and some of them expressly overruled (*People ex rel. United States Aluminum Printing Plate Company* v. *Knight*, 174 N. Y., 475, 485). Some of the statutes prior to 1906 had provided that every domestic corporation should pay a tax "upon its franchise or business", "to be computed" upon dividends declared, or if none were declared, upon the "appraised capital" of the corporation; and that every foreign corporation should "pay a like tax for the privilege of exercising its corporate franchise . . . in this state." These taxes have uniformly been to all intents and purposes direct taxes levied upon the ownership of the corporate franchise or right to do business in corporate form, and not upon the exercise of that right, although the success of the business might determine the amount of the tax. (*People ex rel. United States Aluminum Printing Plate Company* v. *Knight*, *supra*; *Home Insurance Company* v. *New York*, 134 U. S., 594.) They have had in full measure the element of "absolute and unavoidable demand", which is described by this Court in *Flint* v. *Stone-Tracy Company* as lacking in the act of Congress under consideration. The New York franchise tax must be paid by every New York corporation, whether it does business within the State or not, as a condition of the right to continue its

existence (*People ex rel. The American Contracting and Dredging Company* v. *Wemple*, 129 N. Y., 558).

In 1906 the Legislature radically changed the phraseology of the statute so as to read, in part, "for the privilege of doing business or exercising its corporate franchises in this state every corporation, joint-stock company or association, doing business in this state, shall pay", etc.

We shall concern ourselves with only three decisions as to the application of these statutes to receiverships. In *Central Trust Company* v. *New York City and Northern Railroad Company*, 110 N. Y., 250 (decided prior to 1906), a receiver of the defendant (a domestic corporation) had been appointed in proceedings taken to sequestrate its property by a judgment creditor, a statutory proceeding; and afterwards another receiver was appointed in an action to foreclose a mortgage upon the property of the corporation. The question involved was whether the State was entitled to payment of the franchise taxes out of funds in the hands of the receiver in foreclosure. Some of these had accrued before, and some after, his appointment. The Court held that the tax was imposed by the statute upon the "franchise"; that the railroad in the hands of the receiver was operated under and by virtue of the "franchise" and that, therefore, as in the case of taxes imposed upon property, the tax was payable out of the property in the hands of the receiver. Nowhere, however, does the Court define, or refer to other decisions defining, the "franchise" upon which the tax is imposed; but the language of the opinion as a whole leaves no doubt that the Court regarded the act as taxing a collection of rights which may or may not have included the corporate franchise proper, but certainly did include the secondary franchise to run the railway. In this view, however, the New York statute was radically different

from the act here in question, which imposes the tax upon the *use* of the corporate franchise proper, but not upon its ownership or upon either ownership or use of secondary franchises.

In addition to the confusion shown in the opinion as to just what the law taxed, the Court laid considerable stress on the doctrine that the State had paramount rights, inasmuch as it "has succeeded to all the prerogatives of the British crown" and had priority of right in the payment of taxes, a doctrine which was repudiated in *Wise et al.* v. *L. & C. Wise Company*, 153 N. Y., 507. This right has never existed. (*Conrad* v. *Atlantic Insurance Company of New York*, 1 Peter's, 386; *United States* v. *The State Bank of North Carolina*, 6 Peter's, 29; *Savings and Loan Society* v. *Multnomah County*, 169 U. S., 421.)

In the *Central Trust Company* case the Court failed to distinguish between the corporate franchise which the corporation retained, and which was the subject of the tax, and the secondary franchise, which the receiver took and exercised. This same confusion exists in the majority opinion in *New York Terminal Company* v. *Gaus*, 204 N. Y., 512 (decided subsequent to 1906). The plaintiff, a foreign corporation, had purchased at a judicial sale, under a decree foreclosing a mortgage of the Brooklyn Ferry Company, "all of the property of said Ferry Company, corporeal and incorporeal, save the franchises to be a corporation, . . . subject to all taxes which might be a lien thereon, at the time of sale." It was claimed that certain taxes assessed under the above mentioned act, before and after the appointment of a receiver of the mortgaged property of the Ferry Company, were a prior lien on the property purchased. *The question whether the statutes did or did not impose a tax under the circumstances, was not raised, the only question*

being whether it was a lien on the property sold prior to the lien of the mortgage (pp. 514, 519). Gray, *J.*, said (pp. 515, 516):

> "The tax levied by the Controller by virtue of Section 182 *was a tax upon the franchise*, as distinguished from the property of the corporation. It is imposed, as it declares, upon the privilege of carrying on business and of exercising the corporate franchises. . . . We know from the record that the receiver, who was appointed of this corporation, continued to operate its ferry business and that the tax levied during the two years was upon its *franchise, or privilege, to transact such a business*. . . . As he had no individual interest, but only the official possession of the property, *the receiver could only have operated under the corporate franchise*. . . . The corporation was not dissolved; *its franchise to conduct the ferry business* was in existence and any operation must have been by virtue of that franchise. The right of its officers to operate was taken away, for the time, by the Court and was conferred upon the receiver, as its officer. *Operation, therefore, could only have been under the corporate franchise.*"

This language would seem to show beyond question that the majority Judges were treating the tax not as imposed upon the corporate franchise proper—the right to be a corporation—but upon the secondary or special franchise which the corporation already in existence had acquired to run the ferry business. This secondary franchise of course passed to the receiver, and if taxable at all was as readily taxable in his hands as in those of the corporation itself. The language of this Court in the cases cited has, however, made it absolutely certain that the Federal tax under consideration is not imposed upon such secondary franchises.

We respectfully submit that the opinion of Cullen, *Ch. J.*, in which two of his associates concurred, correctly states the law on this subject. He says (pp. 519, 520, 521):

> "A franchise tax is of an entirely different character from a tax on property. . . . It is levied *on the corporation* for the privilege, as the statute declares, of carrying on its business in a corporate or organized capacity (Tax Law, Secs. 182, 184); not of doing business, *but of doing business in a corporate capacity*. . . . The decision below seems to have proceeded on the ground that the right to run a ferry was a corporate franchise granted to the corporation against whose property the mortgage was foreclosed. . . . As a matter of fact many of the ferry privileges, as well as many of the old street railroad franchises in the City of New York, were granted not to corporations but to individuals and their associates. The court below, however, considered that under our statutes individuals cannot own or operate railroads, and that, therefore, the operation of a railroad must be deemed to be under a corporate franchise, and treated a ferry franchise as analogous. If it is possible to settle any question by a uniform current of judicial authority, the settled law is clearly the reverse of the proposition asserted. From the earliest days of railroads corporations owning them have been authorized to mortgage not only the roads but the franchise to maintain and operate them. That necessarily gave to the mortgagees the right to foreclose the mortgage after default, and to the purchasers on the foreclosure the right to operate the road. No legislation could deprive them of that right. But purchasers did not, by the mortgage sale, get the right to operate the road *under a corporate existence*. . . . A receiver appointed in a

> foreclosure suit would take nothing by virtue of the corporate existence of the owner of the equity of redemption, but by virtue of the mortgage."

The record in that case appears to have been very incomplete, and did not disclose what franchises the corporation possessed (p. 520) which may have misled the majority of the court; but even if the view taken by Gray, *J.*, be accepted, the *Gaus* case and the New York franchise tax are distinguishable from the case at bar and the Federal tax. Gray, *J.*, said the New York tax was a tax on the franchise; the Supreme Court in the *Flint* case said that the Federal tax was not a tax on the franchise. The New York law makes the tax a paramount lien on the property of the corporation, a fact upon which great stress was laid in both the *Central Trust Company* case and the *Gaus* case. The Federal Act contains no such provision. The New York tax is imposed in advance based on the amount of capital stock employed during the preceding year, and, therefore, the franchise may not actually be exercised or business actually done during the year for which the tax is assessed. The act does not say capital "employed *by* the corporation" and, therefore, its capital in possession of and employed by a receiver might be taxable. The appointment of a receiver would not change the title to the capital. Under the Federal act there is no tax unless business is actually carried on "by such corporation" "in a corporate capacity," and the tax is based on the income "received by it." It is inconceivable that a court would hold that income received and retained by a receiver of the property of a corporation in a foreclosure or general creditors' suit and which was not turned over to the corporation, was received by the corporation,

even though it should hold that the receiver exercised the franchises of the corporation.

People ex rel. Joline, et al., as Receivers of The Metropolitan Street Railway Company, supra, v. *Williams,* was decided without opinion either by the Court of Appeals or by the Court below. There may have been facts in that case which clearly distinguished it from the *Central Trust Company* and *Gaus* cases. In fact, Cullen, *Ch. J.*, so states in the *Gaus* case (pp. 516, 517).

In *Central Trust Company* v. *Third Avenue Railroad Company,* 186 Fed., 291, it was held that the State of New York was not entitled to a preference (the only point involved in the *Gaus* case) over the Third Avenue mortgage for franchise taxes accruing under this same New York statute. A petition to this Court for a writ of *certiorari* was denied (*The People of the State of New York* v. *Central Trust Co.*, 223 U. S., 721). Therefore, the decisions of the Federal Courts involving the application of the New York statute to receiverships, are diametrically opposed to the three New York decisions cited by the Government.

Whatever the cases referred to above may have held, we respectfully submit that the principle involved in *McCoach* v. *Minehill Railroad Company, supra,* that where the corporation does not actually possess and operate its railroads it is not liable for the tax imposed by the Act of 1909, governs the case at bar; and that furthermore these Receivers did not possess or exercise the corporate franchises of these corporations, but that they operated their railroads solely as officers of the Court, and by virtue of the secondary franchises, and that they are not subject to the Act.

FIFTH POINT.

The decisions of the Circuit Court of Appeals should be affirmed.

EVARTS, CHOATE & SHERMAN,
Solicitors for respondent, Frederick W. Whitridge, as Receiver.

DEXTER, OSBORN & FLEMING,
Solicitors for respondent, Ladd, as Receiver.

JOSEPH H. CHOATE, JR.,
MATTHEW C. FLEMING,
Of Counsel.

In the Supreme Court of the United States.

OCTOBER TERM, 1913.

No. 467.

THE UNITED STATES,

Petitioner,

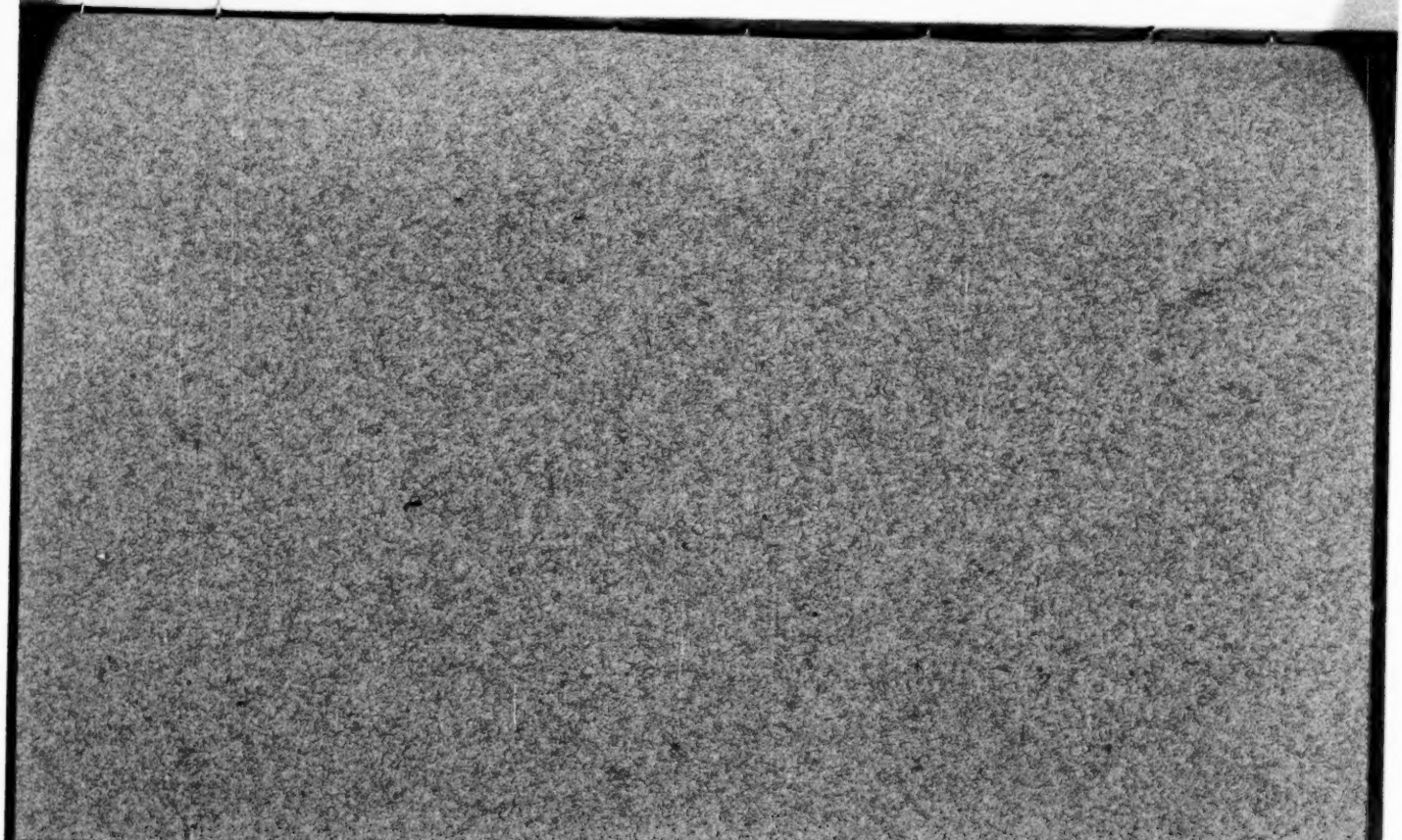
against

ADRIAN H. JOLINE AND DOUGLAS ROBINSON, AS RECEIVERS OF METROPOLITAN STREET RAILWAY COMPANY ET AL.

BRIEF ON BEHALF OF ADRIAN H. JOLINE AND DOUGLAS ROBINSON, AS RECEIVERS OF METROPOLITAN STREET RAILWAY COMPANY.

ARTHUR H. MASTEN,
ELLIS W. LEAVENWORTH,
Counsel.

The Evening Post Job Printing Office, 156 Fulton St., N. Y.



In the Supreme Court of the United States.

OCTOBER TERM, 1913.

No. 467.

THE UNITED STATES,
Petitioner,

AGAINST

ADRIAN H. JOLINE and DOUGLAS ROBINSON, as Receivers of Metropolitan Street Railway Company, *et al.*,
Respondents.

BRIEF ON BEHALF OF ADRIAN H. JOLINE AND DOUGLAS ROBINSON, AS RECEIVERS OF METROPOLITAN STREET RAILWAY COMPANY.

This matter is before the Court on *certiorari* to the Circuit Court of Appeals for the Second Circuit. The decision under review (198 Fed. 774) affirmed a decree of the District Court denying a petition of the United States for an order to direct the Receivers of Metropolitan

Street Railway Company to make and file returns for the years 1909 and 1910, for Metropolitan Street Railway Company, of its net income, pursuant to Sec. 38 of the Act of Congress of August 5, 1909 (36 Stat. L., 112).

The sole question involved is whether an insolvent corporation, the property of which is in the hands of a receiver appointed by a court of equity, in a judgment creditors' or foreclosure action, is "carrying on or doing business" within the meaning of the Act, and whether such receiver is obliged to file a return, under the Act, of his income realized while acting as an officer of the Court.

The Facts.

Metropolitan Street Railway Company is a corporation organized under the laws of the State of New York. Receivers were appointed for this company in a general creditors' suit in the Circuit Court of the United States for the Southern District of New York by order filed October 1, 1907 (Petitioners' Exhibit B, Rec., p. 14), and the same receivers were subsequently appointed for the company in three foreclosure suits in the same court by orders filed October 9, 1907, November 19, 1907, and March 17, 1908, respectively (Petitioners' Exhibits D, E and F, Rec., pp. 18–25). These proceedings were under consideration by this Court in *Re Metropolitan Receivership*, 208 U. S., 90. The Receivers took possession of the

property of the Company on October 1, 1907, and operated it, remaining in sole possession thereof, until the close of the year 1911 (Rec., p. 9). By order filed October 9, 1907, the company, its officers, agents, directors and employees, were enjoined from interfering in any way with the possession or management of the property by the receivers (Rec., p. 17). By order filed November 9, 1907, the company was adjudged insolvent (Rec., p. 7).

At the time when this proceeding was brought (November, 1911) a decree of foreclosure and sale had been entered upon mandate of the Circuit Court of Appeals in the third of the above-mentioned suits, and an appeal was pending from a supplemental decree of foreclosure and sale entered April 6, 1910, in the fourth of the above-mentioned suits (Rec., p. 32). On January 1, 1912, the Receivers delivered possession of the property of Metropolitan Street Railway Company to the purchasers at the foreclosure sales.

For each of the years 1909 and 1910 Metropolitan Street Railway Company, by its vice-president and treasurer, made a return to the Collector of Internal Revenue for the Second District upon a blank form provided for the purpose in which it was stated that during the year in question "the property of this company was in the hands of receivers appointed by a court of competent jurisdiction, who were in charge of its operations; the officers of the company are therefore unable to make this report" (Rec., pp. 25–

28). Under instructions of the court the Receivers made no returns (*Penn. Steel Co.* vs. *N. Y. City Ry. Co.*, 176 Fed., 471, 477).

The Pleadings.

The petition (Rec., p. 6), alleges the organization and corporate existence of Metropolitan Street Railway Company and that

> "in the years 1909 and 1910 *it was engaged in business* in the City, County and State of New York."

It is, however, subsequently alleged (p. 9) that Messrs. Joline and Robinson immediately upon their appointment as Receivers, took possession

> "of all the assets and property of the said Metropolitan Street Railway Company of every kind and nature whatsoever and have ever since remained in possession thereof and have acted and continued to act during the years 1909 and 1910 and ever since pursuant to the terms of each of the said orders appointing them such receivers since the respective dates of entry thereof; and during the years 1909 and 1910 and ever since, *the business of the said Metropolitan Street Railway Company has been done, performed and carried on by the said Adrian H. Joline and Douglas Robinson as such receivers, their agents, employees, etc., and by them alone.*"

It is further alleged that the Metropolitan Street Railway Company became subject by the provisions of Section 38 of the Act of Congress of

August 5, 1909, to pay annually a special excise tax with respect to the carrying on or doing business by such corporation, and the petition then charges (p. 10):

> "That by virtue of the appointment in each of the above-entitled actions of Adrian H. Joline and Douglas Robinson as Receivers as aforesaid of the said Metropolitan Street Railway Company, its assets, property, etc., *the said receivers took the place of the directors and officers of the said company during the pendency of the above-entitled actions to the same effect and with the same liabilities, obligations and duties as were and are imposed by law upon such directors and officers of the said Metropolitan Street Railway Company and more particularly by the provisions of said section.*"

The answer admits the possession and operation of the properties of the Metropolitan Street Railway by the Receivers pursuant to the orders of the Court by which they were appointed, but puts in issue the above quoted allegations of the petition (Rec., p. 31).

I.

The tax is imposed solely upon the privilege of doing business in a corporate capacity. This is apparent from the language of the Act and has been definitely established by recent decisions of this Court.

Section 38 (36 Statutes L., 112) provides:

> "That every corporation * * * organized for profit and having a capital

> stock represented by shares * * * now or hereafter organized under the laws of the United States or of any State or Territory of the United States * * * or now or hereafter organized under the laws of any foreign country and engaged in business in any State or Territory of the United States * * * shall be subject to pay annually a special excise tax with respect to the carrying on or doing business by such corporation * * * equivalent to one per centum upon the entire net income over and above $5,000 received by it from all sources during such year * * *."

This means that the tax imposed by the Act is a tax, not upon business *per se*, but upon the right to do business in a particular manner and with particular advantages, to wit, in a corporate capacity, and with the advantages which inhere in corporate organizations. If business is not done in a corporate capacity, no tax is payable in respect thereto. It is not a tax upon property or franchises or income. Where income is actually received but no corporate business is done, the tax is not payable.

> *Flint* v. *Stone Tracy Company*, 220 U. S., 107;
>
> *Zonne* v. *Minneapolis Syndicate*, 220 U. S., 187;
>
> *McCoach* v. *Minehill and Schuylkill Haven R. R. Co.*, 228 U. S., 295.

II.

The transactions of the Receivers in operating the Metropolitan System during the two years in question involved no exercise of the right to do business in a corporate capacity.

That the Receivers acquired no interest in the right of the Metropolitan Street Railway Company to be a corporation is not open to question. The corporation continued to exist. It could hold corporate meetings and elect officers. It retained title to its property, the Receivers being vested with no interest therein but acting merely as its custodians for the Court. (*Quincy Railway* v. *Humphreys*, 145 U. S., 82.)

It was, however, restrained by the order appointing Receivers from interfering in any way with their management and control of the property. This provision would seem conclusively to dispose of the claim that the administration of the Receivers could involve in any sense the transaction of business in a corporate capacity.

The Government claims, however, that the corporation, although expressly restrained from taking part in the operation of the road, must be regarded as exercising corporate powers because the Receivers could not lawfully have availed of its franchises in the streets. It is pointed out that the Metropolitan Company acquired not only the right to be a corporation but to be a corporation for the purpose of operating

street railroads on certain streets. It is argued (Petitioner's brief, p. 4):

> "Who was carrying on this business if not the corporation? The Receivers could not lawfully do so either as individuals or as officers of the Court. The Court itself could not do so, except by virtue of the jurisdiction it acquired over these corporations having these franchises which alone made such business lawful or possible. It follows by the method of exclusion that it was the corporations who were carrying on the business."

The weakness of this argument is that it fails to recognize the difference between a franchise to exist and a franchise to operate, and it overlooks decisions to the effect that there is no inherent objection to the operation of a railroad franchise by individuals. It is well settled that a corporate existence is not an absolute prerequisite to lawful operation of a railway. This Court said in *Memphis, &c., Railroad Company* v. *Commissioners*, 112 U. S., 609, 619:

> "The franchise of being a corporation need not be implied as necessary to secure to the mortgage bondholders or the purchasers at a foreclosure sale the substantial rights intended to be secured. They acquire the ownership of the railroad and the property incident to it and the franchise of maintaining and operating it as such; and the corporate existence is not essential

> to its use and enjoyment. All the franchises necessary or important to the beneficial use of the railroad could as well be exercised by natural persons. The essential properties of corporate existence are quite distinct from the franchises of the corporation."

To the same effect are

Schurz v. *Cook*, 148 U. S., 397, 409;
Village of Phœnix v. *Gannon*, 195 N. Y., 471.

Nor can the position of the Government be sustained on any theory of trusteeship or agency. It is argued (Petitioner's brief, p. 6):

> "But it is submitted that in every substantial sense the income received and disbursements made by the Receiver are those of the corporation itself. The Receiver takes the income as a trustee, applies it first to the debts *of the corporation* and holds the surplus *for the corporation*. Any net income over and above the expenses, debts, etc., is the equitable property of the latter."

This argument is without force because the question at issue does not turn upon the ultimate rights of the corporation. The right of the Government to collect the tax depends upon whether the Company itself was actually "engaged in doing business." The fact that it may have an equitable or reversionary right to any surplus assets remaining after the termination of the

receivership is immaterial. This is clearly established by the Zonne case (*supra*), in which the corporation sought to be taxed had leased its property for a term of years. This Court said (p. 191) that it

> "was not engaged in doing business within the meaning of the Act. It had wholly parted with control and management of the property; its sole authority was to hold the title subject to the lease for 130 years, to receive and distribute the rentals which might accrue under the terms of the lease, or the proceeds of any sale of the land if it should be sold."

Furthermore, the difference between the business methods of the receivership and those of the corporation itself is so fundamental as absolutely to preclude the application of any theory of agency.

The Receiver represents none of the parties to the cause, but acts under the sole direction of the Court.

> "The contracts he makes or the engagements into which he enters from time to time under the order of the Court are, in a substantial sense, the contracts and engagements of the Court. The liabilities which he incurs are liabilities chargeable upon the property under the control and in the possession of the Court and are not the liabilities of the parties. They have no

> authority over him and cannot control his acts."
>
> *Atlantic Trust Co.* vs. *Chapman*, 208 U. S., 360, 375.

The corporation cannot be deemed to transact business within the meaning of the Act when its property is being operated under conditions which may make a compliance with the requirements of the Act impossible. For example, the corporation in making its return under the Act is entitled to deduct from its gross income the amount of interest paid on its bonded indebtedness. Receivers, on the other hand, rarely pay interest on bonded indebtedness except in the case of underlying liens and therefore would not receive the benefit of this deduction. The corporation is also entitled to deduct from its gross income the amount of current operating expenses. In the case of a receivership such expenses as salaries, counsel fees and fees of Special Masters, are often deferred for several years until the termination of the receivership and then may be paid either from income or from the *corpus* of the property, as occasion may require. It might, therefore, readily occur that an insolvent corporation in the hands of receivers would be subject to a heavier tax than a going concern on the same gross income. Such differences as these are not to be considered mere "administrative details," as counsel for petitioner has suggested. They go to the root of the question involved and show

conclusively that the Court below correctly held that no process of construction would warrant the inclusion of the Receivers within the purview of the Act.

III.

The New York decisions cited in Petitioner's brief are not authoritative.

It is conceded by the Government that they are not binding on this Court, but it is urged that they are entitled to weight on the question of whether a corporation organized under State laws is still doing business under its State charter, although in the hands of a Receiver (Petitioner's Brief, p. 12). We deem it unnecessary to discuss these authorities at any length in view of the recent decisions of this Court on the particular statute now in question. It may be pointed out, however, that each of the cases cited presents features which detract from its weight as an authority on the present issue.

The tax involved in *Central Trust Company* v. *New York City and Northern Railroad Company* (110 N. Y., 250) was held by this Court (*Home Insurance Company* vs. *New York*, 134 U. S., 594) to be a tax upon "the right or privilege given by the State to two or more persons of being a corporation, that is, of doing business in a corporate capacity, and not the privilege or franchise which when incorporated the Company may exercise."

This distinction was not discussed in the Central Trust Company case, the chief point argued being whether or not the franchise taxes then in question were liens upon the property of the corporation. The decision of the Court was to the effect that the Receiver should pay the tax because he had taken possession of all the property of the corporation and operated its trains, thus using the franchise which had been conferred by the State upon the company. To the extent, therefore, that the case treats the franchise in question as the secondary franchise instead of the mere right to do business in a corporate capacity, it is not in accord with the Home Insurance case in this Court.

The decision in *New York Terminal Company* vs. *Gaus*, 204 N. Y., 512, followed the Central Trust Company case and was by a divided court.

IV.

The decision and decree below should be affirmed.

Washington, October 14, 1913.

MASTEN & NICHOLS,
Solicitors for Respondents,
Joline and Robinson as
Receivers.

ARTHUR H. MASTEN,
ELLIS W. LEAVENWORTH,
Of Counsel.